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## Evaluating a Potential US-China Bilateral Investment Treaty: Background, Context and Implications

US-China Economic and Security Review Commission

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# Evaluating a Potential US-China Bilateral Investment Treaty: Background, Context and Implications

## Abstract

[Excerpt] This paper, prepared by the Economist Intelligence Unit for the US-China Economic and Security Council, summarises the context, current discussions and implications of a potential US-China bilateral investment treaty (BIT). The paper is organised in six sections:

- I. Existing US BITs
- II. China's current BITs with other countries
- III. The potential US-China BIT
- IV. Major regulatory and transparency issues
- V. Implications for the US economy
- VI. Interviews

Simply defined, a BIT is a treaty between two countries designed to promote and protect investments between the two signatory states. A BIT provides investors with a safer and more transparent investment environment by guarding against the risk of expropriation by the host state. Many countries, especially the larger economies, sign BITs with their main trading partners, both to ensure that companies from their country receive proper protection when they make investments abroad and to ensure that their rights can be protected and enforced through binding international arbitration.

## Keywords

United States, China, trade, Bilateral Investment Treaty, BIT, investment

## Comments

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# Country & Economic Research

## Evaluating a potential US-China bilateral investment treaty

### Background, context and implications

Prepared for the

US-China Economic and Security Review Commission

Disclaimer: This research report was prepared at the request of the Commission to support its deliberations. Posting of the Report to the Commission's website is intended to promote greater public understanding of the issues addressed by the Commission in its ongoing assessment of U.S.-China economic relations and their implications for U.S. security, as mandated by Public Law 106-398 and Public Law 108-7. However, it does not necessarily imply an endorsement by the Commission or any individual Commissioner of the views or conclusions expressed in the commissioned research report.

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26 Red Lion Square  
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#### **London**

The Economist Intelligence Unit  
26 Red Lion Square  
London  
WC1R 4HQ  
United Kingdom  
Tel: (44.20) 7576 8000  
Fax: (44.20) 7576 8484  
E-mail: london@eiu.com

#### **New York**

The Economist Intelligence Unit  
The Economist Building  
111 West 57th Street  
New York  
NY 10019, US  
Tel: (1.212) 554 0600  
Fax: (1.212) 586 0248  
E-mail: newyork@eiu.com

#### **Hong Kong**

The Economist Intelligence Unit  
60/F, Central Plaza  
18 Harbour Road  
Wanchai  
Hong Kong  
Tel: (852) 2585 3888  
Fax: (852) 2802 7638  
E-mail: hongkong@eiu.com

Website: [www.eiu.com](http://www.eiu.com)

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# Overview

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- I. Existing US BITs
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Simply defined, a BIT is a treaty between two countries designed to promote and protect investments between the two signatory states. A BIT provides investors with a safer and more transparent investment environment by guarding against the risk of expropriation by the host state. Many countries, especially the larger economies, sign BITs with their main trading partners, both to ensure that companies from their country receive proper protection when they make investments abroad and to ensure that their rights can be protected and enforced through binding international arbitration.

There are over 2,500 BITs in operation worldwide today, following on from the first BIT signed between Germany and Pakistan in 1959. Germany has more BITs than any other country (around 140), followed by China, with more than 120; the US has signed over 40 BITs.

Most major economies have their own BIT model. The core elements of the US BIT, according to a recent interview with the US-China Business Council, require the partner-country government to provide US investors with:

- the right to fair and equitable treatment, including neutral arbitration;
- the right to full protection and security, including that provided by international law;
- a non-discriminatory environment compared with domestic investors, based on the principles of national treatment and most-favoured-nation clauses;
- the ability to move capital in and out of the country freely;
- the right to full compensation in the event of expropriation or nationalisation;
- the removal of performance requirements.

China is now established as the leading recipient of foreign direct investment (FDI) in the developing world. It had FDI receipts of just under US\$150bn in 2008 (representing 390% growth on the 2000 figure). A key factor in this growth has been the increase in the overall number and sophistication of China's BITs. China's latest

investment treaties conform to international best practice, giving foreign investors a high level of protection from interference by government.

**BIT negotiations resumed in 2008**

China has signed BITs with most of the world's most significant trading and investing countries, including Japan, Germany and the UK. A major omission is a US-China BIT; discussions were terminated following the Tiananmen Square massacre in June 1989. Rising trade and investment flows between the two nations led them to resume negotiations in June 2008, following the fourth Strategic Economic Dialogue (SED) meeting. The talks have continued under the Obama administration with a new title, the Strategic and Economic Dialogue (S&ED); these will be discussed in Section III.

## I. Existing US bilateral investment treaties

### Introduction

**US BIT programme dates from 1981**

The US BIT programme, initiated by Ronald Reagan in 1981, is intended to encourage and protect US investments abroad, promote the adoption of market-directed policies in other countries and support the development of standards of international law.

As at September 2009, the US was party to 40 active BITs with developing countries in all regions of the world. Several other treaties have been signed by the US but not by the partner country; still others are in the process of negotiation, potentially leading to a formal agreement. Though the first US BIT went into force more than 20 years ago, the US is party to far fewer agreements than other major economies. China, France, Germany, Italy, South Korea and the UK, for example, have signed more than twice the number of BITs as has the US.

The US has BITs with the following countries: Albania, Argentina, Armenia, Azerbaijan, Bahrain, Bangladesh, Bolivia, Bulgaria, Cameroon, Democratic Republic of Congo, Republic of Congo, Croatia, Czech Republic, Ecuador, Egypt, Estonia, Georgia, Grenada, Honduras, Jamaica, Jordan, Kazakhstan, Kyrgyz Republic, Latvia, Lithuania, Moldova, Mongolia, Morocco, Mozambique, Panama, Poland, Romania, Senegal, Slovakia, Sri Lanka, Trinidad & Tobago, Tunisia, Turkey, Ukraine and Uruguay.<sup>1</sup> More information concerning the date these BITs came into force is in Appendix 1.

US BITs, once ratified by both parties, remain in force for ten years. Following the initial ten-year period, either party may terminate a BIT with one year's notice. For ten years following the date of termination, however, the articles contained in the BIT will continue to apply to covered investments made during the time the agreement was active.<sup>2</sup>

<sup>1</sup> List of BITs now in force see [http://tcc.export.gov/Trade\\_Agreements/Bilateral\\_Investment\\_Treaties/index.asp](http://tcc.export.gov/Trade_Agreements/Bilateral_Investment_Treaties/index.asp)

<sup>2</sup> More detail on the 2004 model US BIT discussion can be found at <http://www.state.gov/documents/organization/117601.pdf>.

### **The 2004 model BIT is the starting point for revisions**

All US BITs are based on a model BIT that was last revised in 2004. The model is in the process of another revision, however, by the US Department of State and the Office of the US Trade Representative (USTR), which jointly lead the US BIT programme. A public forum on the matter was held in late July 2009. The major concerns voiced at that time included the following:

- The 2004 model BIT provides weaker protection for US commercial interests compared with the 1994 model
- The current investor-state dispute-resolution process is inadequate.
- The distinction between government regulatory action and indirect expropriation is unclear and, as such, potentially harmful to US commercial interests.
- There is a need to develop enforceable rules within BITs, beyond national regulations, in terms of labour and the environment.
- Restrictions on capital controls in the current model BIT are potentially outdated.<sup>3</sup>

### **The current review of the US model BIT**

It is unclear whether the prospective US-China BIT agreement would be based on the 2004 model or on a new one, since the Obama administration is now conducting a review of the BIT programme. This inter-agency review of the US model is focused on its role as a template for negotiations, and is being conducted concurrent with the BIT negotiations with China, India and other countries. An official at the US-China Business Council in Washington noted in a September 2009 interview that the present goal is to fashion a high-standard BIT, similar to those the US has negotiated with other developing countries. US business groups view this type of BIT as providing the best level of market access, legal recourse, competitive practices and equitable treatment, given China's large state-owned sector.

### **The release of the September 2009 ACIEP report**

In September 2009, at the request of the Department of State and the USTR, the State Department's Advisory Committee on International Economic Affairs (ACIEP) established a subcommittee to analyse the US model BIT. The ACIEP subcommittee's work centred on three areas in particular: dispute-settlement provisions, state-owned enterprises (SOEs) and financial-services issues.

On the matter of dispute settlement, which was the topic of particularly "robust" discussion, subcommittee members were split in several directions. Some members strongly support the investor-state dispute-settlement provisions contained in the 2004 model BIT, arguing that such provisions are contained in almost all of the 2,600 BITs currently in effect and as such provide an "objective, fair and non-politicised forum" for investors seeking redress for breaches of the BIT, and that not using investor-state dispute-settlement mechanisms would put the US at a competitive disadvantage. Other members firmly believe that the international dispute mechanism in the model BIT presents significant risks because international arbitrators working on cases brought under the mechanism may not have a full understanding of local laws and societal values. In addition, some subcommittee members support exhaustion of domestic legal systems before investors have the option to pursue international arbitration, whereas others believe that would be contrary to present international legal practice.

<sup>3</sup> Source: Minutes, July 29th 2009 US Dept of State and USTR meeting.

Regarding SOEs, the subcommittee recommended that the US administration assess whether the model BIT requires countries to ensure that their SOEs accord national treatment and most-favoured-nation treatment to covered investments.

On financial-services issues, where the analysis focused on whether exceptions to the free transfer of capital for covered investments should be made during balance-of-payments crises, the subcommittee was unable to reach consensus. The subcommittee did conclude, however, that a claimant should be permitted to submit claims involving breach of national treatment and most-favoured-nation obligations vis-à-vis financial services<sup>4</sup>.

**President Obama's November 2009 trip to China**

Among the many topics covered in a meeting between President Obama and President Hu of China during Mr Obama's mid-November 2009 visit to China—the nascent global economic recovery, climate change, energy issues, nuclear non-proliferation—were issues related to trade and investment. A joint US-China statement issued following the meeting indicated that “the two sides agreed to work proactively to resolve bilateral trade and investment disputes in a constructive, co-operative and mutually beneficial manner. Both sides will expedite negotiation on a bilateral investment treaty.”

Despite the joint US-China statement issued during President Obama's November 2009 trip that BIT negotiations will be expedited, it does not appear that a US-China BIT will be finalised in the near future. Negotiations are proceeding on a technical, but not yet a political, level. On the matter of politics, some observers note historical difficulties in reaching agreement on foreign investment and trade agreements during an economic downturn. The fact that many members of Congress have voiced concerns about expanding trade and investment linkages with China is also likely to be a hindrance to the US-China BIT winning two-thirds majority support in the Senate.

**Status of the current negotiations**

Should the model-BIT review extend far into 2010, it will delay negotiations with China, since the US needs to have a model treaty solidly in place before moving to finalise specifics of a US-China treaty. During the ACIEP discussions, several business representatives proposed that the committee endorse the 2004 model BIT to expedite finalisation of BIT negotiations with China and other countries—a move that was rejected by representatives of labour unions.

**The US does not have an active BIT with any of the BRICs**

In addition to not having a BIT with China, the United States also does not have active agreements with the other three BRICs (Brazil, Russia or India), the group constituting the world's four largest emerging economies. A BIT with Russia, signed by the US in 1992, has not been ratified by Russia and thus has never gone into force. Discussions on a BIT with India have been underway since 2008, although a formal agreement does not seem likely in the near future. And although formal negotiations towards a BIT with Brazil have not yet begun, the topic was recently addressed at a high-level forum of Brazilian CEOs in Washington, DC. (Brazil is not party to any BITs; its reluctance to accede to such agreements may centre on whether Brazilian law would allow them.)

<sup>4</sup> A number of other topics were covered in the ACIEP report. The report is available at: <http://www.state.gov/e/eeb/rts/othr/2009/131098.html>



A BIT with China, the world's third-largest economy in nominal GDP terms (at more than US\$3.8bn in 2008), would represent by far the largest economy with which the US has a BIT. Turkey, the world's 17th-largest economy (at nearly US\$800m), is now the biggest economy with which the US has an active investment treaty. A US-China BIT would be only the second international investment agreement the US has signed with a major capital exporter.

## Major themes and issues in US BITs<sup>5</sup>

**Reciprocal market access** Under the model US BIT, each party is required to provide investors and covered investments (that is, investments of a company or national of one party of a US BIT in the territory of the other party) "treatment no less favourable than it accords, in like circumstances, to its own investors with respect to establishment, acquisition, expansion, management, conduct, operation, and sale or other disposition of investments in its territory." This constitutes the principle of national treatment. Though market-entry provisions are generally included in any BIT, the US BIT model is unique in that it provides so many levels of post-establishment protection to investors.

Additionally, the US model BIT contains an article on most-favoured-nation (MFN) treatment that provides the same protections for BIT-partner countries as it does, in like circumstances, for countries with which it does not have a BIT. In general, US BITs require the use of the more favourable of national or MFN treatment for investments of the other party.

In the US-Turkey BIT, which entered into force in 1990, Turkey insisted that MFN treatment be used for the establishment of investments. In practice, this means that all subsequent stages in the life cycle of an investment (acquisition, expansion, etc.) are undertaken using the more favourable of national or MFN treatment. The same qualification was used in the US-Morocco BIT.

**Expropriation and nationalisation clauses** The model BIT also provides clear protection against expropriation or nationalisation of an investment (by either party) except for public purpose, which must be undertaken in a non-discriminatory manner and with "prompt, adequate, and effective compensation." For expropriation, the model BIT specifies that compensation must be made at the fair market value of the expropriated investment immediately before the date of expropriation and that compensation must include interest. The annexes to individual BITs spell out further terms regarding a potential expropriation.

In the US-Turkey BIT, the language on expropriation was revised to say that interest on an expropriated investment be repaid at the "government borrowing rate" rather than at a "commercially reasonable rate".

**State, local and county-level rules** US BITs as well as investment chapters of US free-trade agreements (FTAs), such as NAFTA's Chapter 11, provide certain standards for foreign-investment protection. Article 2.1 of the model BIT stipulates that national or federal governments can be

<sup>5</sup> Information in this section is based on the text of the 2004 model US BIT found at: <http://www.state.gov/documents/organization/117601.pdf> and individual US BITs found online at: [http://tcc.export.gov/Trade\\_Agreements/Bilateral\\_Investment\\_Treaties/index.asp](http://tcc.export.gov/Trade_Agreements/Bilateral_Investment_Treaties/index.asp)

liable for breaches of these standards even when these arise from actions taken by state, provincial and county-level governments.

There may indeed be circumstances in which a foreign investor could sue the US government for monetary damages under a BIT based on a local government's restrictions that prevent the investor from obtaining the intended benefits of its investment. Under many US BITs, this is done by submitting a claim to an independent, international arbitration tribunal indicating that the local government's actions breached one or more standards of foreign-investment protection in the BIT. *[More discussion of this issue can be found in the section on arbitration processes on p. 10.]* The claim would be for monetary damages for harm to the investor or the investment. The case would be made that there was an issue or breach of the following:

- National Treatment: If local regulations were uniquely applied to foreign investors, there could be a BIT violation;
- MFN treatment: If local regulations applied to foreign investors from one country and not from another, there could be a BIT violation;
- Minimum Standard of Treatment: Tribunals have reached different conclusions about what constitutes the minimum standard of treatment; a BIT violation could occur if government regulations were imposed in a way that abused due legal process or denied justice to the foreign investor (such as for sham administrative or legal proceedings);
- Expropriation: The investor might have a valid BIT claim if government regulations constituted an expropriation of the foreign investor's property, and the expropriation (a) was not done for a public purpose; (b) was done in a discriminatory manner (for example, simply because the investor was foreign); (c) did not result in adequate and effective compensation paid in a timely manner; or (d) was without due process of law.

### **Capital transfers**

Within the confines of the 2004 US model BIT, article 7 obliges both the US and the partner country to permit the transfer of capital related to a covered investment (profits, dividends, capital gains, proceeds from the sale of an investment and several other categories) "freely and without delay", and in to and out of its territory at the market exchange rate. Recently, however, there has been much discussion of whether the US should revise this article to allow for exceptions to free movement of capital during balance-of-payments crises. Large current-account and capital-account imbalances between the United States and China and the possibility that these imbalances may contribute to future balance-of-payments instability point to the likelihood of serious consideration about such exceptions during US-China BIT negotiations.

Some language on capital transfers has been adjusted. Because of Turkey's concerns about the volatility of its exchange rate, for example, the US-Turkey BIT states that "in exceptional financial or economic circumstances related to foreign exchange", Turkey may delay the transfer of proceeds from the sale or liquidation of an investment until foreign-exchange reserves have risen to a more acceptable level, and that the delay may extend up to three years.

### **Strategic sectors and the “negative list” approach**

Active US BITs do not address which sectors are more or less important than others in terms of investment. Instead, they employ a “negative list” approach, specifying which sectors are off limits for partner countries. If the US does not list a sector, the other BIT party presumably has the right to invest in it at will.

In the US-Panama BIT, for example, the US includes on its negative list, among other sectors, air transport, shipping, banking, insurance, broadcasting, telephone services and satellite communications. Panama, likewise, limits investment in many of the same sectors.

In the US-Uruguay BIT, the first signed following the 2004 revision of the model text, the US placed limitations on investments in the air transport, banking, insurance, mining, radio/satellite communications and cable-television sectors, among others. Uruguay puts limitations on investments in sectors such as air, rail, road, and port infrastructure and services; financial services; water and gas; fisheries; and radio and television.

### **The role of CFIUS**

Outside the realm of BIT stipulations, the Committee on Foreign Investment in the United States (CFIUS) reviews foreign investments in the US. In recent years, review and rejection by the CFIUS of a number of major proposed investments has caused tension with several countries, including China.

Whether a US-China BIT takes a “negative list”, a “positive list” or some other approach towards sectors open to mutual investment, the general sentiment among observers of the US-China BIT negotiations is that the US will insist that a BIT *not* limit national-security (that is, CFIUS) reviews of proposed investments currently in place. That said, pending foreign investments in the US are submitted for review CFIUS on a voluntary basis. However, CFIUS does have the power to review pending investments that are not submitted.

By some accounts, a US-China BIT could be an opportunity to strengthen the principle of non-discrimination of Chinese investment in the US compared with other countries’ investment in the US.

### **Performance requirements**

The US model BIT prohibits the imposition of performance requirements, including domestic-content targets, export and import quotas, and technology transfer (among other areas) as a condition for the establishment, acquisition, expansion, management, conduct, operation or sale of an investment covered under a BIT.

In some instances, such as in the BIT with Panama, exceptions have been made. The US-Panama BIT allows Panama to grant benefits to investors under its established incentive laws.

### **Labour and the environment**

The model US BIT contains clauses regarding both environmental and labour concerns. The clauses indicate that it is “inappropriate to encourage investment by weakening or reducing the protections afforded” in domestic environmental and labour laws, adding that labour laws include regulations related to the rights of association and collective bargaining, prohibition of forced labour, labour protections for children and young people, and acceptable work conditions. The model BIT does not, however, establish environmental or labour restrictions in addition to existing national laws.

**Arbitration processes**

US BITs encourage initial efforts at dispute resolution to be made through consultation and negotiation between the claimant and respondent. Disputes that cannot be resolved through that process are settled under procedures established by the World Bank's International Centre for the Settlement of Investment Disputes (ICSID), assuming both the claimant and defendant countries are party to the ICSID Convention. If a dispute is not resolved through consultations or diplomatic channels, government-to-government dispute settlement (that is, in national courts) would still be available to investors that encounter trouble.

Some BITs have been revised to capture shifts in arbitration procedures. The US-Uruguay BIT contains two such annexes: the first bars US investors from submitting certain types of claims under BIT channels that have already been submitted before a Uruguayan court or administrative tribunal; and the second bars investor cases claiming that a "negotiated restructuring" of a sovereign-debt instrument breaches any obligation under Section A of the BIT except national and most-favoured-nation obligations.

In another instance, at the time of the 1982 US-Panama BIT (which entered into force in 1991), Panama was not party to the ICSID Convention, and the agreement was signed using the ICSID Additional Facility as the forum for arbitration. Following Panama's accession to the ICSID Convention, the BIT was amended in 2000.

During the early days of the North American Free-Trade Agreement (NAFTA), parties within the US were concerned that the use of international tribunals in cases brought by foreign investors under free-trade agreements (FTAs) and BITs would open the US to a deluge of claims. Further criticism surrounded the fact that, in contrast to US judges, the international tribunals were beyond the reach of US democracy and that many of the arbitrators would be foreign nationals with the power to render monetary judgments against the US government—the damages of which would ultimately be paid with taxpayer revenues. Such fears have proven unfounded. In the more than 15 years since NAFTA entered into force, there have been only 15 cases brought against the United States, not one of which has required the US to pay a monetary award.

Michael Snarr, counsel at Baker Hostetler, interviewed for this paper, describes an example of the process of bringing a property dispute by a foreign investor against the US as follows: "As for raising the BIT in court, the challenge would not be to a trade court. The US Court of International Trade has a special, limited jurisdiction and would not have jurisdiction over a claim property dispute with a local, state or federal government, even if an argument were made about a BIT. Even if one were to go to a regular US federal district court, the case likely would be dismissed because the BITs or FTAs are explicit in limiting the rights of private persons to invoke the obligations in those agreements to the dispute-settlement mechanisms contained in the agreements. In other words, the district court would say that to the extent a foreign investor may claim any relief under the BIT, such relief is provided explicitly through the arbitration mechanisms in the agreement and not to be applied in US courts except to enforce an arbitration award rendered by a tribunal under the agreement."

**Ratification process  
in the US**

Negotiation and ratification of US BITs follows a linear process. First, the US secretary of state authorises the negotiation process. Negotiation with the partner country on the terms of the individual BIT then proceeds. Once the two countries' negotiators come to agreement on the terms and the secretary of state authorises the transmittal, the BIT goes

to the president for signature. Following presidential signature, the Senate Foreign Relations Committee considers the treaty, reporting its findings to the full Senate. The BIT then requires approval by a two-thirds majority in the Senate, at which point it enters into force. It is not uncommon for the elapsed time between the president's signing of the treaty and Senate's ratification of it to be several years, and for that period to straddle presidential administrations.<sup>6</sup>

## Impacts of BITs

Overall, US BITs open channels for US companies to develop and expand their commercial interests internationally. BITs pave the way for US companies to set up export-distribution networks, provide services directly through branch and affiliate offices *in situ*, and engage in research and development to meet the demands of local needs while expanding sales markets. US BITs have positive effects on partner countries: US companies invest with more confidence (especially in countries that have had weak foreign-investment-protection measures); it opens bilateral communication channels on trade and investment; and these channels may lead to future agreements, such as a bilateral free-trade agreement.

An analysis of US BITs with developing countries shows that when BIT agreements are in force (compared with those signed but awaiting ratification), there is an observable positive effect on the increase of inflows of US foreign direct investment (FDI). One such study, conducted at the University of Illinois at Chicago, examined investment-flow data from 1977-2004. This study shows that an active BIT increases the level of US FDI to a partner country, whereas a US BIT that is signed but not yet in force does not. There is often a two-to-three-year gap between the time an agreement is signed and the time it comes into force.

Because of data constraints, it is difficult to examine the effect of BITs on FDI into specific sectors. Research in 2005 found that a higher number of BITs increases FDI flows into a developing country. Though the finding that BITs in some manner increase the level of FDI between signatories is the most common outcome of such studies, other reports reach different conclusions. One recent analysis, for example, finds "little evidence that existing international agreements—trade and investment framework agreements (TIFAs), BITs or preferential trade agreements (PTAs)—tend to increase investment in partner countries from the United States."<sup>7</sup> Data available from the US Bureau of Economic Analysis is included in the dataset accompanying this report.

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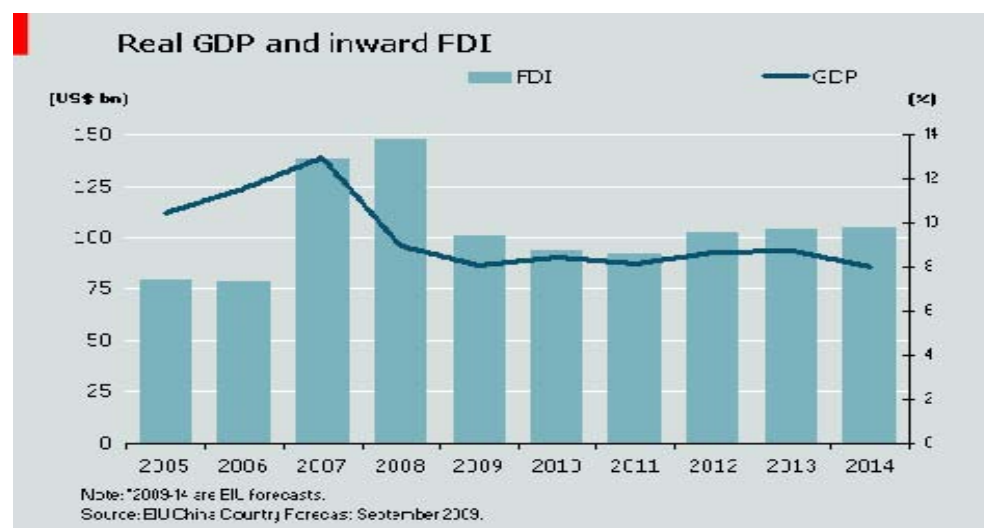
<sup>6</sup> [http://www.unctad.org/en/docs/webiteia20069\\_en.pdf](http://www.unctad.org/en/docs/webiteia20069_en.pdf)

<sup>7</sup> See [http://psweb.sbs.ohio-state.edu/intranet/gies/Haftel\\_GIES.pdf](http://psweb.sbs.ohio-state.edu/intranet/gies/Haftel_GIES.pdf); [http://papers.ssrn.com/sol3/papers.cfm?abstract\\_id=616242](http://papers.ssrn.com/sol3/papers.cfm?abstract_id=616242) and <http://www.asil.org/files/jelconferencepapers/peinhardt.pdf>

## II. China's current BITs with other countries

### Introduction

China has emerged in recent years as the leading destination in the developing world for foreign direct investment (FDI). Moreover, China is also an increasingly important source for outward FDI, especially for developing countries in Africa, Latin America and Asia. Less-well noticed, however, has been the fact that China has now signed more than 120 bilateral investment treaties (BITs) with other countries, ranking second in the world after Germany. These treaties are increasingly regarded as crucial not only for foreign investors in China, but also for Chinese companies investing abroad, providing them with the confidence to invest overseas without the risk of expropriation.



### Chronology of China's BITs

China's approach to BITs has changed significantly over the years, and the country's BIT policy can be divided into three different periods. The first stage was from 1949 (with the foundation of the People's Republic of China) to 1981, the start of the period of openness and reform. During these years, China adopted an aggressive and hostile approach to foreign direct investment (FDI) and BITs in line with its overall ideology, including an opposition to concepts of private property. During this period, expropriations were frequent and without compensation.

The second stage, 1982-97, witnessed a change in China's attitude towards foreign investment, as the country opened up to the rest of the world following more than 30 years of economic isolation. Eager to attract FDI, economic development became a priority for the government. As a result, China signed its first-ever BIT with the government of Sweden in 1982. Over the next 15 years, attitudes towards FDI evolved as the level of legal protection for foreign investors gradually increased, and by mid-

1998 China had signed a total of 80 BITs. Despite this, the overall level of protection offered in these BITs was still fairly low.

Since 1998, China has entered into increasingly sophisticated BITs. Indeed, China has now signed BITs with most of the world's capital-exporting countries, including the UK, Japan, Germany and France. There is no BIT in force with the US; negotiations were terminated in 1989 following the Tiananmen Square massacre. Reflecting China's increasingly important role as source of FDI in the developing world and the demand from Chinese companies for greater protection for their overseas investments, China has also now signed BITs with many developing countries in Asia, Africa, Eastern Europe and South America.

As China has overcome its traditional and long-held scepticism towards international law, China's BITs since 1998 have increasingly followed international best practice, and they are comparable to those found in more developed countries. These BITs provide a high level of protection to foreign investors, as well as unlimited access to dispute-settlement mechanisms, provisions on most-favoured-nation treatment and national treatment of foreign investors. This includes the recent high-profile BITs signed with the Netherlands in 2001 and Germany in 2003.

## Major themes and issues in China's BITs<sup>8</sup>

### Arbitration

China was initially reluctant to consent to arbitration as a way to settle disputes in its BITs. Indeed, the first BIT with Sweden contained no investor-dispute provisions at all. But the lack of an effective and working arbitration process undermined the effectiveness of the BITs as a means of investor protection.

This changed following the signing of a new generation of BITs in the late 1990s, when China began to agree to a proper dispute-settlement mechanism. The first BIT that provided for genuine dispute settlement was signed with Barbados in 1998. The fact that the first such BIT was signed with a developing country is significant: it implies that pressure from Chinese investors, concerned about the lack of protection they receive when investing abroad, might have persuaded the Chinese government to change its stance and to allow proper access to arbitration. An arbitration clause was also included in the June 2000 BIT signed with Botswana, when China consented to allow for international arbitration "for any dispute between an investor of one Contracting Party and the other Contracting Party" either through an ad hoc tribunal, or through the ICSID Convention.

Dispute-resolution provisions were included in other BITs with developed countries, including that signed with Germany in 2003, whereby "any dispute concerning investments shall at the request of the other contracting state be submitted for arbitration". Under the terms of this arbitration, investors are given the right to have their case referred to the World Bank's International Centre for Settlement of Investment Disputes (ICSID). Under ICSID, dispute resolution is fully

<sup>8</sup> Information for this section was drawn from a number of sources including: <http://jiel.oxfordjournals.org/cgi/content/abstract/jgp020>, <http://www.asil.org/files/teleconferencepapers/berger.pdf>, <http://law.bepress.com/expresso/eps/1928>, and <http://www.amchamchina.org/article/4135>.

comprehensive, and member states must “recognise an award ... as binding, and enforce it ... as if it were a final judgment of a court”.

*More discussion of this issue can be found in Section IV, p. 33.*

**Most-favoured-nation treatment** The most-favoured-nation (MFN) treatment clause has been included in all of China’s most recent BITs. The inclusion of this clause has important implications, since under the MFN China is obligated to extend all the benefits of its new-generation BITs to countries that signed the more restrictive, old-generation BITs.

The MFN clause aims to create a more equal and competitive landscape for all foreign investors regardless of nationality. This clause is especially important given that China’s most recent BITs grant substantially more access and protection to foreign investors, yet signatories of the old-generation, more restrictive BITs can now enjoy these benefits.

**National treatment** Traditionally seen as one of the core guarantees provided in modern BITs, the extension of national treatment implies the creation of a level playing field for foreign and local investors alike to ensure fair and equal competition. Under national-treatment provisions, governments must ensure that foreign governments provide equal treatment to foreign investors and that there is no discrimination on the grounds of nationality.

China’s pre-1998 BITs typically did not include full national treatment. This reflected a determination within the Chinese government to promote Chinese companies as “national champions” and to ensure that the government could maintain as much control over the economy as possible. It was also a recognition that Chinese companies would struggle to compete against more-sophisticated, world-class companies.

The first BIT to include a mention of national treatment was the China-UK BIT of 1986. Even under the terms of this BIT, however, the provision was included whereby “the Contracting Party shall to the extent possible, accord (national) treatment”. The inclusion of the phrase “to the extent possible” was designed to ensure that no binding restrictions would be imposed.

China’s newer generation of BITs, from 2001 onwards, began to include stricter national-treatment provisions, starting with the BIT signed with the Netherlands. Even in this case, though, there were still qualifications ensuring that the provisions were not completely binding.

Indeed, China finally agreed to grant full and unqualified national-treatment provisions without reservations only for the BIT with the Seychelles, which was signed in 2007. The decision to allow national treatment was a major development in China’s BIT practice, and it has served to underline China’s increasing commitment to BIT best practice. It has also served as a mechanism to enforce the continued opening of the domestic economy to foreign competition.

Significantly, since all of China’s BITs include most-favoured-nation clauses, the concessions offered in the Seychelles BIT are available to all foreign investors.

**Security protection** A security-protection guarantee is standard in China’s BITs and requires the state to provide protection against physical interference—such as rioting and



demonstrations—in the host country. This guarantee is especially valuable for less-stable regimes in Africa, where destruction of physical assets is more likely to be a problem.

**Protection against expropriation**

Protection against expropriation is an especially important guarantee in China, following the large-scale seizure and nationalisation of foreign assets after the Chinese Communist Party came to power in 1949. Although expropriation is much less likely to be an issue for foreign investors at the moment, the guarantee is included in all China's BITs.

**Amount of compensation**

China's old generation of BITs did not often adhere to best practice in the area of compensation, which under the most modern and comprehensive BITs demands "prompt, adequate and effective compensation". China's new-generation BITs have clarified this issue. The 2003 China-Germany BIT, for example, requires that "compensation shall be equivalent to the value of the investment immediately before the expropriation is taken" and that the "compensation is paid without delay and shall carry interest." Foreign investors remain concerned, however, over the calculation of the exact level of compensation under China's present BIT terms.

**Capital transfer**

In China's old generation of investment treaties, capital-transfer provisions were strict by design. China aimed to ensure control over all foreign exchange entering and exiting the country in order to maintain control over the exchange rate. Yet the country increasingly recognised that capital-transfer restrictions were not compatible with the goal of encouraging FDI into the country, since companies are unwilling to invest in a country that does not allow repatriation of profits. Capital-transfer provisions were gradually eroded, and in the 2003 China-Germany BIT they were broken altogether, allowing for unlimited capital transfer. Most-favoured-nation provisions also add to the scenario for foreign investors with their concurrent favourable provisions.

**Capital movement and profit repatriation**

Foreign investors can open and maintain foreign-exchange accounts if approved by the State Administration of Foreign Exchange (SAFE). SAFE will determine the amount of foreign exchange that a company needs; deposits exceeding this level must be converted to local currency. Authorised foreign investors can retain foreign exchange equivalent to 50% of their export earnings. China now has a relatively liberal approach, allowing foreign investors to repatriate legally earned profits if the company involved can produce the appropriate paperwork. Foreign businesses in China rarely mention the issue as a major problem, which may be partly because most companies in China reinvest the vast majority of their earned profits in their China-based ventures. Nevertheless, the government has gradually been stepping up its monitoring of some of the channels used to repatriate profits, which has raised the administrative burden associated with these paths. Transfer pricing, for example, is increasingly subject to regulatory scrutiny to ensure that intra-company pricing is reasonable; some companies think that the authorities' judgment of what is reasonable is at odds with their own. Another example is royalty payments. As mentioned elsewhere in the report, some foreign investors have reported that the government is putting pressure on them to reduce royalty payments, registering more intellectual property in their China-based vehicles. Capital-account transactions are more tightly restricted under China's closed capital-account system, and they require case-by-case approval. As a result, foreign investors report that receiving regulatory approval for injections of capital to expand businesses can sometimes be difficult (especially if the authorities are trying to limit inflows of liquidity into the economy from abroad).

**Umbrella clause** One of the most controversial aspects of BITs has been the introduction of the so-called “umbrella clause”, now included in about half of all of China’s BITs. Most BITs cover areas such as the violation of national-treatment provisions and expropriations, which typically involve protection against interference from government power. However, there are many cases where an investor may be more concerned about the willingness of another company, and not of the government, to fulfil its contractual obligations.

Protection against commercial breaches of contract can be covered under the umbrella clause of a BIT, which according to the Germany-China BIT stipulates that “each Contracting Party shall observe any other obligation it has entered into with regard to investments in its territory by investors of the other Contracting Party”. Although China was traditionally wary of allowing such clauses into its BITs, the new-generation BITs typically include such provisions.

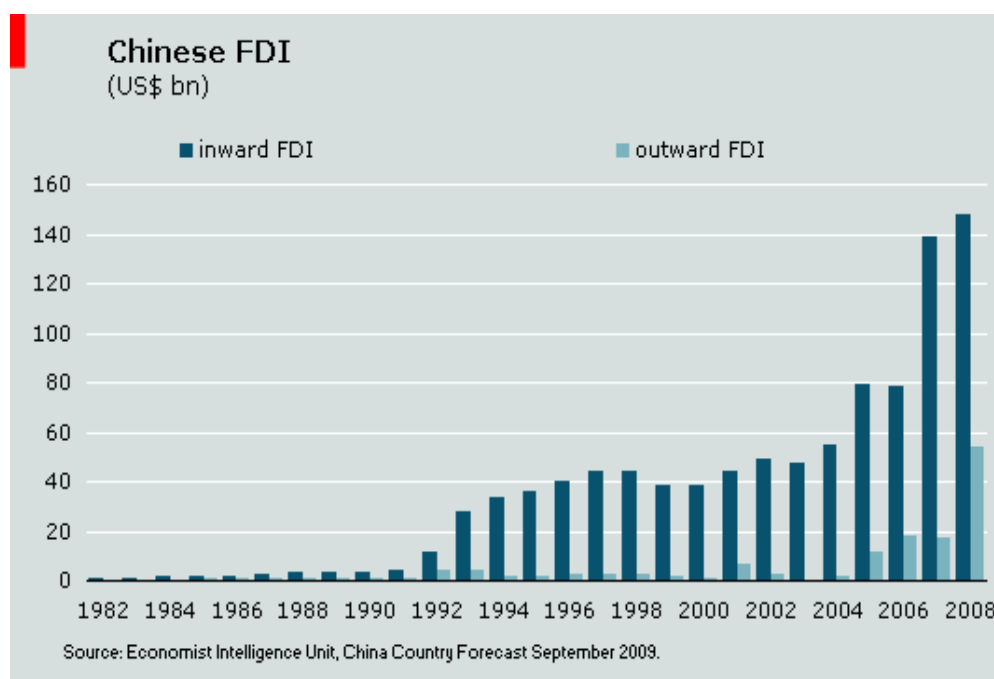
The clause means that a foreign investor can take to arbitration any company in breach of an investment contract. This provides significant benefits to a foreign company, which will be able to depend on a transparent, international-dispute-resolution mechanism, rather than on the local Chinese arbitration courts, which have been criticised as slow and lacking in transparency.

## Impacts of BITs

As noted earlier, the level of inflows of foreign direct investment (FDI) into China have increased rapidly in recent years, making China the largest recipient of FDI in the developing world. FDI inflows into China were just US\$400m (on a balance-of-payments basis) in 1982, increasing to US\$11.2bn in 1992, US\$44.2bn in 2001 (the year of China’s entry into World Trade Organisation), and then to a record US\$147.8bn in 2008. Meanwhile, outward FDI, which was just US\$44m in 1982, grew to US\$913m in 1991 and US\$6.9bn in 2001; it has ballooned over the past couple of years, reaching US\$17.8bn in 2006 and a record US\$53.4bn in 2008.<sup>9</sup>

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<sup>9</sup> Data for this section from National Bureau of Statistics.



Inflows of FDI into China have increased for a number of reasons:

- the increasing number and sophistication of China's BITs;
- explosive growth in China's economy, which has encouraged more companies to invest in the country as a way to access the booming domestic market;
- China's low labour costs (see table on the next page), efficient workforce and improving infrastructure, which has allowed China to establish itself as a manufacturing export power-house, attracting billions of US dollars in FDI from foreign companies in the process;
- China's entry into the World Trade Organisation in late 2001.



The investment environment in China has greatly improved since the country's WTO accession in December 2001, tariff reductions have been implemented on schedule and most market-access measures are in operation. As a result, a significant number of markets have been opened to investment. In the banking sector, for example, restrictions on local-currency business by foreign banks have been eased, and geographical and customer restrictions on renminbi services have been removed.

Foreign companies involved in logistics and distribution have expanded their business scope, with restrictions lifted on foreign ownership for freight forwarding, warehousing and other operations. The protectionist telecoms sector has also seen major changes, with foreign-equity limits raised. In addition, regulatory restrictions on foreign investment in tourism were lifted as from July 1st 2007, in line with China's WTO commitments to allow foreign travel agencies to set up branch offices nationwide. Since 2004, foreign investors have also been allowed to take full ownership of hotels.

China's entry into the WTO in 2001 has also driven changes in the pharmaceuticals sector, where innovative pharmaceutical companies can now carry out research and development (R&D) because of fewer concerns over poor intellectual-property protection. Foreign investment in this sector has boomed, and most of the world's largest foreign companies have established R&D centres in China. These companies include GlaxoSmithKline and AstraZeneca (both of the UK), Roche and Novartis (both of Switzerland) and Bayer (of Germany). However, the foreign pharmaceutical company with the biggest presence in China is Pfizer (of the US), which has a total staff of around 4,000 and production plants in Dalian, Suzhou and Wuxi. Overall, Pfizer has invested more than US\$500m in China. Significantly, all of this has occurred in the absence of a US-China BIT; suggesting that not having a BIT signed and enacted with China does not present a huge obstacle for foreign companies. The same is also true in China's automotive sector, which has received billions in foreign investment in recent years, and where one of the biggest investors has been General Motors (also of the US).

Aside from the United States, China has signed BITs with most of the world's developed countries. The emphasis most recently has been on signing BITs with less-developed countries, especially oil- and commodity-rich countries in Africa and Latin America that can provide much needed inputs for China's booming economy. From the perspective of a Chinese company, many of which have little experience investing in foreign countries, the increased confidence and legal support available through a BIT (giving Chinese companies the right to appeal for international arbitration, for example, in the event of the expropriation of a mine in a foreign country) explains much of the surge in outward FDI by China to the developing world in recent years.

**WTO Commitments<sup>10</sup>** The US Trade Representative (USTR) released its annual report in late December, assessing how well China is doing in meeting the commitments it signed up to as part of its WTO accession agreement of 2001. Although the overall message of the report was mixed, and though some "concrete results" had been achieved over the past year, big concerns remained on how well China is complying with its WTO obligations. The main complaint focused on concerns that China is not taking adequate measure to enforce its own intellectual-property laws, despite a number of anti-piracy campaigns that it has launched in recent years. Altogether, the USTR estimates that US software and music companies suffered losses of around US\$3.5bn as a result of poor enforcement of the laws.

The report was also critical of other aspects of China's trade regime. In agriculture, where China has generally met all of its commitments, US companies still suffered from unpredictable practices, which in 2009 led to shipments of agricultural products from the US being held up at customs in China. China was also guilty of limiting market access for foreign companies, such as through the inclusion of the "Buy China" policies included in the government's stimulus package, along with complicated new standards in telecommunications, which were designed for the benefit of Chinese telecoms companies. The USTR report was also critical of China's new postal law, which the report claims excludes foreign companies from a "significant" part of the rapid-delivery market in China.

## Conclusion

Although the Chinese government has traditionally been slow to grant significant rights to foreign investors that could be enforced through international arbitration, this is now changing. The past few years has seen a number of developments to China's BIT regime. These changes have significantly extended the protections offered to foreign investors in China from interference from the government.

Although China signed a number of BITs in the 1980s and early 1990s, it was not until the late 1990s that the basis for the present agreements emerged. With China's role as a leading destination for foreign direct investment, and with growing demands by the international community for greater foreign-investment protection, the country eventually agreed to comprehensive expansion of the protections offered to investors.

China's most recent BITs are now comprehensive and include all of the rights found in the most substantive BITs in force around the world today. These include the following:

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<sup>10</sup> See [http://www.ustr.gov/webfm\\_send/1572](http://www.ustr.gov/webfm_send/1572) for more information.

- protection against expropriation and discriminatory action from the government;
- unhindered transfer of profits back from China;
- the right of investors in China to start binding-arbitration proceedings against the government, which can be enforced by the World Bank.

### III. The potential US-China BIT

#### Key issues

##### **Intellectual-property protection**

China continues to make progress in fighting intellectual piracy<sup>11</sup>. However, the degree of protection of intellectual piracy remains well below the level that most of its trading partners expect, and this is likely to remain a major source of dispute. Piracy problems are still common in almost every sector of the Chinese economy, including media, software, electronics, industrial goods, consumer goods, pharmaceuticals and food products. Indeed, the US Trade Representative (USTR) estimated that 85-93% of all copyright products sold in China in 2007 were pirated, showing little improvement over the previous year.

Despite the poor level of overall intellectual-property-rights (IPR) protection, China has not stood still in its efforts to address the IPR issue. Since joining the World Trade Organisation in December 2001, Beijing has worked hard to strengthen its IPR regime, including the revision of major laws on patents, copyrights and trademarks in line with the requirements of the Trade-Related Aspects of Intellectual Property Rights (TRIPs) agreements of the WTO. China is already party to several other major international conventions on IPR. The government has issued numerous official notices and amendments on specific areas, such as pharmaceuticals, Internet domain names and software piracy. In some, especially where these involve trademark infringement, solid remedies are available against infringers, and the situation continues to improve, especially in large urban areas. Patents, too, can often be effectively protected, though the enforcement procedure is tortuous. However, copyright protection, especially for music, films and computer software, remains a weak area.

Although the range of enforcement options open to victims of piracy in China continues to increase, the reality is that even though the central government wants to stop counterfeiting, its ability to enforce rules, especially in remote regions, is limited. Factors that hamper enforcement efforts include local protectionism, insufficient manpower and the absence of effective deterrent measures.

##### **Fragmented regulatory environment**

Moreover, the situation is unlikely to change soon for several reasons, including the following major issues:

<sup>11</sup> Intellectual-property-protection information derived from the Economist Intelligence Unit's China Hand: [http://portal.eiu.com/index.asp?layout=displayIssueTOC&toc2=no&issue\\_1024946887&publication\\_id=870003687](http://portal.eiu.com/index.asp?layout=displayIssueTOC&toc2=no&issue_1024946887&publication_id=870003687).

- Toothless agencies: most lack the funding—and often the willpower—to implement laws;
- Costs of litigation: the costs and complexities of pursuing counterfeiters through China's legal system are often prohibitive;
- Lack of training, and inadequate, non-transparent processes.

More generally, it is hard to escape the conclusion that enforcement of intellectual-property rights is a low-priority issue for most government officials.

### **The trade balance**

The US is by far the largest of China's trade partners, with a relationship that is also the most problematic. China's massive trade surplus with the US is a strain on bilateral relations. Nonetheless, under the Clinton and Bush administrations, the US maintained a policy of "strategic dialogue", with both presidents arguing that it is better to talk with China than confront it. The Obama administration has begun a review of the process but is unlikely to change this overall stance.

Chinese statistics traditionally underestimate the size of Sino-US trade, as they do not distinguish between direct exports and transshipments through Hong Kong, whereas US statistics overestimate the size by combining both figures. Regardless of which statistics are used, the bilateral trade deficit between the US and China grew rapidly in 2005-08. However, the size of the bilateral trade deficit is forecast to shrink over the next few years, with import growth into the US likely to be blunted by the need for households to rebuild their savings, following a collapse in property and share prices over the past year. Meanwhile, continued strong growth in China (albeit down from the levels in 2003-07) should support relatively buoyant import growth in that country.

The US government will continue to press for a much greater appreciation of the Chinese currency this year, which it cites as the main cause of the bilateral trade deficit. However, American criticism of China will be blunted by the need to win the latter's support in several areas, not least in budget financing—China was the top buyer of US Treasury bonds in 2008. Meanwhile, the Chinese will be reluctant to allow a rapid appreciation of the currency amid concern on how this would affect the competitiveness of its exports.

The US Trade Representative's annual report to Congress on China's WTO compliance, released in December 2008, maintained the relatively conciliatory note struck the previous year. While noting the various areas in which China continues to fall short, it also emphasised the progress made in bilateral talks, which had improved the access of US companies to Chinese markets for agricultural and other products.

The Chinese government abandoned the renminbi's decade-old fixed exchange rate in July 2005, when it revalued the currency by 2.1% and replaced the peg to the US dollar with a managed float. The move came in response to strong pressure from the US government and a booming trade surplus.

### **The RMB exchange rate**

Despite strong pressure from China's main trading partners to allow the renminbi to appreciate faster against the US dollar, the Chinese currency has remained fixed against the dollar since July 2008. The Chinese government will probably remain very cautious in the operation of its exchange-rate policy, and it is highly unlikely to bow to pressure from trade partners for a large-scale revaluation or even a faster rate of appreciation. The Economist Intelligence Unit forecasts that, as part of a gradual

tightening, the government will adjust its policy stance, allowing the renminbi to resume a slow but steady rise against the US dollar from around mid-2010 onwards. Despite the problems that it causes for exporters, appreciation of the renminbi is desirable, as it should help to cut the huge surpluses on China's capital and current accounts, which are contributing significantly to global economic imbalances. A BIT agreement between China and the US would give the US no extra leverage over China's exchange-rate policy. Indeed, the BIT negotiations would not be the best forum for the US to pressure China on the exchange rate. Instead, these discussions should occur during the Strategic and Economic Dialogue (S&ED) negotiations.

The US government and China's other main trade partners have consistently argued that the renminbi is undervalued. In making these arguments, they have pointed to three factors, namely China's huge foreign-exchange reserves, the country's vast current-account surplus and the fact that goods in China are still much cheaper than in the US. The US and China's other major trade partners may put further pressure on the Chinese government to allow faster appreciation of the renminbi. However, China's crucial role in resolving the ongoing global financial crisis means that both the EU and the US will be careful not to alienate the Chinese authorities through the use of threats.

There remains significant debate within the Chinese government over the rate at which the government should allow the currency to rise. The Ministry of Commerce, for example, would prefer to see a much slower rate of appreciation in order to support exporters. Despite the problems that a faster appreciation rate may cause for exporters, a further rise in the value of the renminbi is desirable since it should help to cut the huge surpluses on China's capital and current accounts, which are contributing significantly to current global economic imbalances. By cutting the cost of imported goods, the renminbi's appreciation should also help the rebalancing of China's domestic economy, by encouraging private consumption. But the government will remain wary of the potential social costs of a continued strengthening of the renminbi, and in the event of a major slowdown in economic growth, the pace of appreciation may be slowed or possibly even reversed.

### **Environmental standards and regulations**

By almost any standards, China's environmental problems are severe<sup>12</sup>. Air and water pollution, water scarcity, desertification, land contamination and health problems among residents of heavily polluted areas are major issues. China's cities are among the most polluted on earth, with the country home to 16 of the 20 most-polluted cities in the world, according to the World Bank. Water pollution is just as serious a problem. This is exacerbated by the fact that only around 50% of urban sewage is treated, and some 278 of China's 661 cities had no sewage-treatment plants as at end-2005.

The prevailing political culture and regulatory structures have exacerbated environmental problems. One of the features of China's economic boom over the past decade and a half has been a rapacious growth-first mentality among businessmen and politicians. With officials largely rewarded for attracting investment and delivering strong economic growth, this has led to the approval of countless projects without due regard for their environmental impact. Simply put, China's present position is

<sup>12</sup> Economist Intelligence Unit: Asia Regional Overview, July 2006 article by Mary Boyd, found at <http://www.eiu.com>.



unsustainable. Without more-efficient use of energy and water, its environmental problems will worsen as the economy continues to grow rapidly and as per-capita prosperity rises.

China's government is unquestionably paying closer attention to environmental sustainability. Thus far, however, it has failed to meet the main targets for reducing pollution, and structural constraints continue to hamper it. The most fundamental change is that an environmental agenda is now more clearly articulated in high-level policy. The 11th Five-Year Plan (covering 2006-10) emphasises sustainable GDP growth and the quality, not quantity, of economic output. The plan sets specific environmental targets, including for energy efficiency, discharges of major pollutants, forest cover, as well as improvements in the efficiency of industrial and agricultural water use, and more waste-water treatment.

China is doing a lot to tackle its environmental crisis, but it faces a colossal task. The central government recognises the seriousness of the situation and is adjusting policy accordingly. But whether it has the ability and political will to effect change on the scale needed is far from certain. For one thing, though spending has increased, China is not spending enough money; the government invested only 1.3% of GDP on environmental-protection treatments in 2005, still below the 2% recommended by the World Bank.

Nevertheless, efforts to introduce cleaner technology, to reduce emissions and to increase penalties for environmental transgressions will continue to gain momentum. At the same time, a drive to increase massively the use of nuclear power and renewable energy sources will continue. More progress would be possible if China improved its institutional framework. It should aim to consolidate supervisory agencies and give more power to key bodies such as the Ministry of Environmental Protection (MEP), the main environmental-regulatory authority.

Foreign-invested enterprises (FIEs) face the same environmental and building restrictions that apply to domestic enterprises—though many complain that they face more-rigorous enforcement of the rules. Part of the official rationale behind such double standards is that foreign companies have longer experience with environmental protection and should therefore meet stricter requirements. State-owned enterprises (SOEs) generally pose a far greater threat to the environment, but realistically, SOEs are probably too well connected with local authorities to face strict requirements on a level anywhere near the ones imposed on FIEs.

**Service access (film,  
entertainment and  
broadcasting)**

China's film, entertainment and broadcasting sector remain largely off-limits to foreign investors.<sup>13</sup> Liberalisation of this sector will probably lag behind others. Indeed, following China's entry to the WTO in 2001, the film and media sector was one of those that remain most protected from foreign competition. The restrictions facing foreign companies in this sector are wide-ranging, including a restriction that allows just 20 foreign films to be legally shown in China each year; a sophisticated Internet firewall that prevents most western news websites from being viewed in China; and a media business (including radio and TV stations, newspapers, magazines and film production) that is largely off-limits to foreign companies.

<sup>13</sup> Information for this section is drawn from <http://www.amchamchina.org/article/4135>.

Although the government claims that these restrictions are in place to protect China's domestic companies from foreign competition, the reality is that the media sector in China is viewed as being too politically sensitive to be thrown completely open to foreign companies. The government's overwhelming priority is to maintain social stability; this is achievable only if the government can maintain a tight grip on all public access to information. As a result, the liberalisation of this sector will probably lag significantly behind the rest of the economy.

**Labour standards** Labour standards are improving across China, and the country already has a number of pieces of legislation in place designed to protect worker's rights in the country.<sup>14</sup> However, although China has introduced much new legislation in recent years, the unhealthy relationship between corrupt local officials and local businessmen will remain the main stumbling block in the path of progress on labour rights. China also has only a patchy ability to implement existing law. Breaches are often investigated only when senior officials order action; the realities of the political system heavily compromise efforts by the police and other agencies that are meant to detect illegal behaviour.

The most important piece of labour legislation China has introduced in the reform era is the Labour Contract Law (LCL), which took effect on January 1st 2008. The new law replaces one put into place in 1995. Although China has emerged since then as an attractive manufacturing base, concerns have grown over poor labour conditions—hence, the new law that, on paper, dramatically changes the balance of power between workers and employers

Companies will need written contracts with all full-time employees, and anyone who works for more than four hours a day will probably be considered a full-time employee. Once they are full-time, employees who are laid off must be bought out at a multiple of their average monthly salary. It is permissible to make more than 20 employees, or 10% of the workforce, redundant, but this must be done on the basis of seniority, not merit. The law is supposed to provide greater job security. Workers with ten years or more of service will have open-ended contracts, and companies will have to inform unions before sacking anyone. Employers fear the law will mean bigger severance payments.

The new law has been a boon to the All-China Federation of Trade Unions (ACFTU), an umbrella organisation for all China's unions, which in many ways acts as an arm of government. But the ACFTU it has seen its power eroded in recent years as state-owned industries have collapsed and the private sector has flourished, eschewing niceties such as unions and Communist Party cells. Despite strong claims by the ACFTU, it is not expected to emerge as a new champion of workers' rights. Independent trade unions will remain in effect illegal; China has no plans to reintroduce the right to strike, which it abolished in 1982.

One of the main complaints is that the new law does nothing to improve the lot of tens of millions of migrant workers from the countryside. They make up most of the unskilled labour in urban areas and are the most frequent victims of poor labour conditions. China's official trade unions have yet to build a network among such workers. Moreover, many companies will continue efforts to evade the law or else

<sup>14</sup> Source: Economist Intelligence Unit's China Hand.

simply ignore it. Moreover, the law was introduced in mid-2007, when the economy was still growing strongly and many companies could afford the increased provisions. However, the sharp economic downturn at the end of 2008 (which has left many companies struggling to survive) has meant the enforcement of the law can be described as patchy at best.

**Financial market access**

Following China's entry into the World Trade Organisation, foreign banks have gradually been allowed greater scope for their investments in permissible business and geographical areas. Foreign banks, long limited to doing business in local currency with foreign companies, were allowed to conduct business in the local currency with Chinese enterprises as from December 1st 2003. They gained access to renminbi business with local individuals in December 2006. Foreign banks' geographical scope for renminbi business was fully liberalised in late 2006.

Nevertheless, it will be cumbersome for foreign banks to take full advantage of the opening of the banking sector mandated by the WTO. Under these rules, foreign-funded or joint-venture banks will have to incorporate in China with registered capital of Rmb1bn (US\$145m). For each branch they open, they will have to allocate another Rmb100m in operating capital. The WTO agreement also specifies that foreign financial institutions, in order to be allowed to do renminbi business, must have a three-year record of accomplishment for operations in China and must have been profitable for two consecutive years prior to application.

## July 2009 Strategic and Economic Dialogue

The latest incarnation of US-Chinese talks, which took place in Washington DC on July 27th-28th, emphasised both sides' hopes for greater co-operation, but they ultimately agreed upon little of substance.<sup>15</sup> The US-China Strategic and Economic Dialogue, as these subtly renamed talks are now called, produced a memorandum of understanding on climate change and routine statements of commitment to free trade, balanced economic growth and security co-operation. But despite the lack of specific measures, the tone of the talks was encouraging. It suggests that the US and China recognise their increased mutual dependence and see the value of being less combative in future discussions.

Emphasising the rising profile of Sino-US relations, the talks opened with a speech by Barack Obama. The US president stressed the importance of increased co-operation between the world's sole superpower and the world's fastest-growing major developing country. The new talks supersede the Strategic Economic Dialogue format launched in 2006, adding an "and" to the title to highlight a shift in focus from purely economic issues to a broader range of economic, environmental and diplomatic topics. Whereas the old format was spearheaded, on the US side, by the Treasury department and focused on resolving economic disputes between the two countries—most notably over China's exchange-rate policy—the new talks had a strong foreign-policy angle as well. This was visible in the prominent involvement of the US secretary of state, Hillary Clinton, in addition to the Treasury secretary, Timothy Geithner.

Relaunching the talks with a broader agenda reflects unspoken recognition that the old format did not work that well. In part, this may have reflected Chinese frustration with

<sup>15</sup> Information derived from <http://ustreas.gov/initiatives/us-china>.

the US's fixation on a single issue—the exchange rate—and a feeling that the supposed “dialogue” was more like a twice-yearly lecture on currency policy. However, the fall-out from the global financial and economic crisis has made it harder for the US to advocate its economic world view, and there is a chance that the new Strategic and Economic Dialogue could offer more genuinely two-sided debate.

#### **Climate change and global warming**

A key focus of discussion in Washington was global warming and climate change. China's booming economy, huge population and energy-intensive, inefficient industrial sector have made the country the world's largest emitter of carbon dioxide. As a result, China is now central to any global climate-change initiative. There is growing recognition in China's government of the seriousness of the country's own environmental problems, as well as of the potentially dramatic consequences of failing to halt global warming. Nevertheless, China's central role in the search for a co-ordinated multilateral solution to global warming will probably be awkward, given the concurrent need for China's leadership to sustain rapid economic growth. This dilemma has big consequences for international co-operation. China (along with India) is strongly opposed to any plan that would impose binding emissions targets on all countries. China has argued that since developed countries are historically responsible for the high levels of carbon dioxide already in the atmosphere, they should pay the majority of the costs of any clean-up. This attitude, despite its undeniable logic, will make even harder the task of finding a viable solution to the problem of climate change.

The United States, under President Obama, is committed to combating climate change, but it is well aware that any global solution must involve not just the US (and other developed economies) but also China and other large developing countries. Although the positions of developed and developing countries remain entrenched, China will not want to be labelled the world's environmental villain.

Unsurprisingly, given the two countries' continuing differences, there were no major agreements at the Strategic and Economic Dialogue. But the two sides signed a memorandum of understanding committing to more bilateral discussions in future. Both the US and China are keenly aware of the importance of achieving progress at the UN climate-change summit in Copenhagen later this year. That said, China is unlikely to make substantial concessions in terms of targets in Copenhagen.

#### **North Korea**

Possible co-operation over North Korea was also high on the agenda in Washington. The US is increasingly concerned over the irrational behaviour of North Korea, which carried out another nuclear test on May 25th and subsequently tested a number of short-range missiles. The US would like China, North Korea's one-time close ally, to exert more pressure on the regime. From China's viewpoint, North Korea's behaviour is increasingly embarrassing. Although China's influence over North Korea is often overstated, China alone has the economic leverage to force the regime back to the negotiating table. Amid concerns in China that the threat from North Korea may encourage Japan to abandon aspects of its pacifist constitution, China may consider putting more pressure on North Korea. However, China remains concerned over the implications of regime collapse in North Korea. This could result in a massive humanitarian crisis, with hundreds of thousands of starving North Koreans streaming over the border into China. This concern, and the fear in China that tougher measures on North Korea could exacerbate the regime's erratic belligerence, means that China is not likely to exert as much pressure as the US would like.

**Economic rebalancing**

Of the economic issues that were discussed, the most important was the rebalancing of Chinese GDP growth away from its traditional dependence on exports and investment. The US hopes that if the Chinese economy is driven more by private consumption, it will boost Chinese import demand and help to lift the US and other economies out of recession. The Chinese increasingly recognise that the growth model that has served China so well in the past (a cheap currency, strong exports and super-powered investment growth) will not be viable until the US and EU economies recover their previous vigour. Even then, it will be in China's long-term interest to achieve more-balanced growth.

China is gradually introducing measures to support private consumption, such as the establishment of a comprehensive social-security system (which should help reduce consumers' incentive to save). However, these measures will take many years to be effective, and are unlikely to have much effect on supporting demand in the short term. Meanwhile, the Chinese government has shied away from bolder measures, such as allowing a faster appreciation of the renminbi. A big revaluation of the local currency would lift consumers' real purchasing power and give companies an incentive to shift resources into production for the domestic market. However, with exports still plunging, policymakers in China are reluctant to let the renminbi rise too fast.

Also high on the agenda at the forum was the safety of Chinese investments in the US. This comes amid concern that record low interest rates in the US, and the country's huge fiscal deficit, will eventually lead to the re-emergence of inflation, hitting the value of China's investments. Owing to China's exchange-rate policy, which has seen the renminbi closely track the US dollar, the value of China's foreign-currency reserves exceeded US\$2trn in the second quarter of 2009, after the Chinese government was forced to intervene in foreign-exchange markets to prevent the renminbi from appreciating against its US counterpart. Although such measures have enabled the US to keep interest rates low, they have left the Chinese holding an estimated US\$800bn worth of US Treasuries, the value of which is vulnerable to a fall in the US dollar or to the re-emergence of inflation.

**No discussion of the renminbi**

The latest Strategic and Economic Dialogue may end up being remembered not for what was discussed, but for what was not. Whereas discussions of the renminbi and China's mounting trade surplus with the US dominated previous meetings, those issues barely figured this time. This is despite the fact that the renminbi has not appreciated at all against the US dollar over the past 12 months, having been stuck at Rmb6.83:US\$1 since July 2008. The US has traditionally blamed the "under-valued" Chinese currency as a major cause of the US trade deficit, and of the global imbalances that arguably contributed to the current crisis. The fact that this issue did not feature reflects the lack of economic leverage that the US now has over China, and the US's dependence on Chinese purchases of its debt to fund its huge fiscal deficit. The Americans remain aware that a decision by China to allow its currency to float freely would necessitate less Chinese intervention in foreign-exchange markets. This could lead to a sharp rise in US interest rates, which would risk deepening the US recession.

*Obama visit in November 2009*<sup>16</sup>. US President Barack Obama paid his first visit to China on November 15th-18th 2009, and though the BIT talks were not the focus of the trip, both sides did agree to expedite the negotiations. Despite Mr Obama's visit, trade frictions between the United States and China have continued to rise. The overall tone of Mr Obama's visit to China was of an increasingly assertive China listening, but clearly not paying much heed, to US concerns. The US president's addresses were not televised live in the country, whereas China delivered a volley of demands and criticism of its own.

The meeting between the US president and China's top leaders may have built a base for future improvements in relations. Optimists note that Mr Obama's strategy of limiting to private discussions criticism of China's policies in areas such as human rights may be more productive than public dressings-down. However, the two sides were able to point to remarkably few areas of agreement on the main issues of controversy, such as China's exchange-rate regime and its policy towards Iran, or US tariffs on Chinese products, such as tyres. A few minor deals were reached on promoting co-operation in fields such as space exploration and measures to tackle climate change, but these represented unimpressive results for so high profile a visit.

## Areas of controversy

The negotiations between the US and China over a BIT are likely to be long and tortuous. As with the negotiations for China's entry to the WTO in 2001, the US will probably demand a number of wide-ranging concessions from China. At the same time, however, China has emerged as an increasingly important investor in the US and will itself demand some concessions from the US before any agreement is made. There are three issues, however, that look to cause the most amount of disagreement and controversy.

### Committee on Foreign Investment in the US

China is growing increasingly concerned that its investments in the US are being hampered by national-security restrictions. Under the terms of the Committee on Foreign Investment in the United States (CFIUS; an inter-agency committee of the United States government), all foreign investments into the US are reviewed in order to consider their national-security implications for the US. This follows the failure in 2008 of a US\$2.2bn bid for 3Com, a US Internet equipment maker, by a Chinese company, Huawei Technologies. The bid failed over concern in the US government over Huawei's relationship with China's military and government. The failed bid drew comparisons with the high-profile failure, also on national-security grounds, of the attempt in 2005 by China National Offshore Oil Corp (CNOOC) to take over Unocal, a US oil company, in a deal valued at US\$18.5bn.

The failure of these deals sent the message that these large national companies are considered to be controlled by the Chinese Communist Party (CCP), and as such are potential tools for the Chinese government in achieving its strategic objectives. There was concern that allowing the CCP access to a strategic energy source such as oil (as in the CNOOC case), or sensitive information technology (as in the Huawei example) would have constituted a national-security risk.

<sup>16</sup> [http://www.economist.com/world/asia/displaystory.cfm?story\\_id=14915086](http://www.economist.com/world/asia/displaystory.cfm?story_id=14915086).

## **Government procurement**

Protectionism in the area of government procurement is another issue that may cause controversy in the negotiations. This follows the unveiling of massive fiscal-stimulus packages in both the United States and China in order to support their economies during the current global economic downturn, and the appearance of “Buy America” and “Buy China” clauses in their respective fiscal-stimulus packages, which raised concerns over each country’s commitment to free trade. Despite the controversy caused by the appearance of the “Buy China” clause, Chinese law at present allows government purchasing from foreign suppliers only under “exceptional” circumstances.

Under the terms of China’s accession to the World Trade Organisation in 2001, it promised to apply to join the government-procurement agreement (GPA; a trade pact that prevents member countries from discriminating against each other’s goods and services in government-procurement projects). Despite these promises, China is now only into its second year of negotiations to join the GPA. China appears in no great rush to join, since the present system allows the government to discriminate in favour of Chinese companies when giving out contracts under its own US\$586bn fiscal-stimulus package. The government would be very reluctant to give up this system, since it lets the government influence and promote certain strategic sectors, such as technology and energy, by awarding certain big contracts to favoured companies.

## **Market-economy status**

The risk of rising protectionism from the US (following President Obama’s decision to impose tariffs on imported tyres from China) will make China increasingly keen to secure market-economy status (MES) from the US. On joining the WTO in 2001, China agreed to be recognised as a transition economy for 15 years before automatically being granted MES in 2016. Eight years after China’s accession, some 79 countries have already granted it MES. However, the US, EU and Japan have not done so. Without MES, it is easier for countries to bring anti-dumping cases against China. Under WTO rules, most countries can be found guilty of dumping if they export products at lower prices than those charged in their domestic markets. But because of China’s status as a transition economy, when WTO members try to determine market rates for Chinese goods, they can use costs from “surrogate” trading partners, which usually have higher production and labour costs than China. This almost invariably causes Chinese prices to appear artificially low, making dumping allegations easier to prove.

China embarked on a high-profile campaign in 2004 to persuade its trading partners to recognise it as a market economy, citing the economic reforms that it has implemented. China was especially piqued that Russia, which has still to be admitted to the WTO, has been accorded MES by the US in its ongoing WTO application process. Indeed, it appeared as though the EU was ready to grant China MES in 2009, but it gave up owing to objections from the US. Having made little progress, China appeared to have abandoned its mission and concentrated its efforts on negotiating bilateral free-trade agreements with individual countries or regional groupings. However, the Chinese once again appear keen to gain MES. At the recent Strategic and Economic Dialogue between China and the US in July, the US promised to “consult through the JCCT” (Joint Commission on Commerce and Trade).

## IV. Major regulatory and transparency issues

### Introduction

China's World Trade Organisation accession protocols, as noted in the previous section, were a landmark for the country's trade relations with other nations, but they also provided a significant boost to the liberalisation of China's investment environment. Tariffs on inputs were substantially reduced; local-content requirements and mandates to export a proportion of production were—for the most part—withdrawn; many new industries were completely opened up to foreign businesses, and in others, the caps on their holdings in joint ventures were raised. Despite this, the regulatory system governing investments remains generally weak, plagued by inconsistent application of standards and laws, numerous grey areas within existing legislation and a lack of transparency within the system. Many foreign investors perceive a widespread and growing degree of discrimination on the part of official agencies that favours domestic businesses<sup>17</sup>.

Advocates of a Sino-US BIT argue that it would provide new avenues and new authority for companies to address these issues<sup>18</sup>, and they hope that it could transform the local investment environment. Clearly, a high quality BIT would bring many advantages. Not least, these could potentially include extra protection against expropriation, the liberalisation of restrictions on corporate transfers of funds, the removal of content and technology-transfer requirements on investments, and access to international arbitration in cases of disputes between businesses and the sovereign.

Nevertheless, as significant disputes remain over China's implementation of its WTO accession promises, so too a BIT would be unlikely to remove all current sources of disagreement. BITs do not tend to cover all fields in detail, and the burden of proving breaches of treaty commitments can be difficult. Fundamental clashes will also remain between the push from businesses to liberalise the investment environment and the policy agendas of the two governments. On the Chinese side, there exists a determination to build companies able to compete at the global level and a desire, on the part of the government, to retain control over the "commanding heights" of the economy, not least to aid macroeconomic policy management. These ambitions favour state-owned enterprises (SOEs) especially. Moreover, both the US and China share a desire to protect strategically important sectors, such as defence, from investments that might undermine their sovereign authority.

Regarding the US, many in China feel that this position has been taken too far, with the review process of the Committee on Foreign Investment in the United States (CFIUS) serving as a block to investments—for example, Huawei's attempted buy an interest in 3Com—that are politically rather than strategically sensitive. Although

<sup>17</sup> For example, the 2009/10 European Chamber of Commerce in China Position Paper notes that "European companies believe that their Chinese competitors are benefiting from infrequent audits or—in many cases—not being audited at all. This discretionary application of environmental regulations amounts to a hidden subsidy for non-compliant Chinese companies".

<sup>18</sup> Interview Erin Ennis



some US parties share this view, a large constituency in the US also feels that the CFIUS review system is an essential tool for safeguarding national security, so adjustments to the system would be controversial.

Although a BIT cannot resolve all the regulatory complications facing businesses investing in the two nations, it may still be able to make a positive contribution in many areas. The extent of any improvement in the business environment created by a BIT will obviously depend on the type of agreement signed. The traditional BIT forms adopted by the Chinese and US governments differ significantly, making it particularly hard to judge the possible benefits that may be gained. The analysis below looks at some of the main regulatory and transparency issues that a Sino-US BIT might address, and it attempts to flesh out some of the possible implications that a treaty could have if agreement in these areas might be reached.

## Key findings

### Expropriation

Protection from expropriation is one of the most standard elements of any BIT. Standard US and Chinese BITs include clauses that provide for swift, transferable and fair-market-value compensation for investments that are expropriated, and both require that the process is to be done in accordance with the law.

Nevertheless, this clause would not be without controversy. The biggest disagreement would probably emerge over the concept of indirect expropriation—that is, where an action has an effect equivalent to direct expropriation, even without the transfer of title or outright seizure. In standard US BITs, this is explicitly addressed (for example in Annex B of the Rwanda-US BIT); in Chinese ones, it is not addressed—although exceptions such as the China-India BIT of 2006 do address indirect expropriation, in terms that seem to have borrowed from the US model BIT<sup>19</sup>.

In China's case, indirect expropriation is a particular concern, owing to a number of situations that are already on the horizon. US companies are concerned over a provision in China's anti-monopoly law (AML), which came into force in 2008, that allows for compulsory licensing of intellectual property (IP) if abuse of monopoly authority occurs. The American Chamber of Commerce in China has noted:

“The AML does not, however, clarify the distinction between legitimate exercises of IP rights and abuses. US companies are particularly concerned that unsound approaches to market definition may lead to findings that IP holders are “dominant” in markets for their own technology and that their unilateral refusal to license their IP to competitors or charging of royalties commensurate with the commercial value of their IP may be condemned as abusive”<sup>20</sup>.

As China's policy makers seek to address the challenges facing them, the temptation to resort to compulsory licensing might well be strong. Would a technology company like Qualcomm be forced to provide access to its technology, for example, to help China move up the value chain? Less commercially aggressive examples are also

<sup>19</sup> Cai Congyuan, China-US BIT negotiations and the future of investment treaty regime: a grand bilateral bargain with multilateral implications, p.22

<sup>20</sup> American Business in China 2009 white paper p.39

conceivable. The compulsory licensing of medical intellectual property (IP) to address a medical crisis has already been seen in many emerging countries like Thailand and Brazil as they dealt with AIDS: if China faced an emergency viral outbreak, it too could feel obliged to resort to compulsory licensing. In addition, there has been some speculation that environmental technology could come under compulsory licensing as part of an effort to address China's emissions. For these reasons, US businesses would view provisions to protect against indirect expropriation as an important part of any high-quality BIT.

Direct expropriation of intellectual property is, of course, also a concern for US companies in China. In AmCham-China's 2009 Business Climate Survey, 72% of respondents viewed enforcement of IP rights as ineffective, despite some recent incremental improvements. Some 12% found it "totally ineffective"<sup>21</sup>. In so much as appropriation is carried out by the government, or by government-linked entities and individuals, cases could be brought under a BIT seeking remedy for appropriation of IP. To take hypothetical examples, if a Chinese state-owned enterprise was producing pirated Microsoft software or manufacturing cars using IP stolen from GM, a case could theoretically be brought for redress under a BIT. In practice, however, such behaviour is already illegal. Poor enforcement and weak punishments for violators of the law are among a number of lingering obstacles preventing an improvement in IP protection. Although a BIT might strengthen the IP environment by allowing investors to bypass the local legal system and go to international arbitration, its effectiveness would be partly determined by the conditions stipulated in the treaty. If the document required that investors first attempt to seek redress via the local regulatory system, its effect in this field might be muted.

#### **National treatment and MFN status**

China is a relative newcomer to the concept of national treatment (that no discrimination should exist between the treatment of investments by domestic and foreign parties)<sup>22</sup>. Although there were some exceptions (notably with developed-nation treaties) through the 1980s and 1990s, most of China's BITs merely adhered to the most-favoured-nation (MFN) principles—that is, investments by companies from the BIT signatories would receive treatment no less favourable than that accorded to any third party.

Even since 1998 when this practice seems to have changed, China has often inserted clauses that weaken the strength of the national-treatment provision. For example, the China-Botswana BIT of 2000 precedes the commitment to national treatment with the phrase "without prejudice to its laws and regulations", which "limits the effectiveness of the national-treatment provision to a best-effort clause"<sup>23</sup> (see endnotes for source). Although there is often some contrast between the treatment China offers to developing countries and that available to OECD governments, in the latter case too China still tends to hedge its bets on national treatment. Its 2005 BIT with the Czech Republic, for example, contains an exemption (seen in a similar form in many other recent BITs) for any existing regulation that does not conform to national treatment, as well as the continuation and even the possible amendment of non-conforming

<sup>21</sup> American Business in China 2009 white paper p.39

<sup>22</sup> Axel Berger, China's new bilateral investment treaty programme: Substance, rationale and implications for international investment law making, p.9

<sup>23</sup> Ibid, p.12

legislation. China makes a commitment to “take all appropriate steps in order to progressively remove the non-conforming measures”<sup>24</sup>, but in practice many observers feel that there has been little effort to adhere to this legal platitude.

Although national-treatment and MFN clauses have not proved so far to be a means for removing existing discriminatory treatment, it is possible that they could serve as a useful tool for preventing the imposition of further discriminatory treatment. As foreign companies in China become more concerned about the risk of unequal treatment, and as new industries potentially emerge in future, this could become an important argument in favour of a BIT with China. In addition, under the MFN clause, countries that have secured a BIT can be reasonably confident that they will enjoy any benefits that subsequent negotiations deliver to other investor nations if China makes further concessions in future.

### **International legal protection and fair and equal treatment**

The fact that a BIT gives an investor a legal-party status and the ability to take a foreign government to international arbitration is among the treaty’s most fundamental benefits. US companies have won awards in a number of cases challenged under BITs—for example, Duke Energy’s successful claim against Ecuador in 2008<sup>25</sup>. Particularly for a country like China, which is very cautious about giving up any aspect of its sovereignty, granting the right for a company to take it to an international court is no small step. Indeed, following growing concern among Chinese officials about the vagueness of fair-and-equal-treatment conditions, some recent bilateral economic treaties have begun trying to provide more clarity. On the positive side, some of these efforts are drawing it closer to US practice: in the China-Mexico BIT of 2008, Article 5 on minimum standards of treatment draws from the US 2004 BIT Model on fair and equal treatment<sup>26</sup>.

For US firms in China, the right to fair and equal treatment with Chinese investors will be among the most important aspects of this legal protection. It is true that Chinese courts have sometimes ruled against local authorities in legal cases. Nevertheless, such examples are few and far between, and given that the legal system is explicitly subservient to the Chinese Communist Party, it would be hard to envisage the courts ruling against the central government in a high-profile case. China is of course not the only country where foreign businesses would feel more comfortable taking their cases to an unbiased international tribunal. Fair-and-equal-treatment clauses are among the most relied upon clauses in claims by investors under BITs—and also among the most successful<sup>27</sup>.

One particular field of equal treatment worth highlighting relates to denigrating publicity campaigns. In 2008 the *Biwater v Tanzania* case saw a tribunal rule that a series of public announcements denigrating the investor’s poor performance and announcing that a new public entity would be taking over the service were in violation

<sup>24</sup> Article 3, Agreement between the Czech Republic and the People’s Republic of China on the promotion and protection of investments

<sup>25</sup> UNCTAD, Latest Developments in Investor-State Dispute Settlement, IIA Monitor No.1, International Investment Agreements, p.7

<sup>26</sup> Cai Congyuan, China-US BIT negotiations and the future of investment treaty regime: a grand bilateral bargain with multilateral implications, p.13

<sup>27</sup> UNCTAD, Latest Developments in Investor-State Dispute Settlement, IIA Monitor No.1, International Investment Agreements, p.8

of the fair-and-equal-treatment standard—even given the investor’s poor record, due process was found to be due<sup>28</sup>. Given state-control over the media, and the country’s tendency to launch campaigns against foreign companies in the press before they reach the courts (for example, the recent anti-bribery case concerning Rio Tinto), a BIT might provide useful support. Nevertheless, other tribunal judgments have stressed that their decisions must take into account the circumstances prevailing in the host state, which investors would have taken into consideration when making their investment.

### **Role of BIT in challenging policies favouring SOEs**

Within China, there are a number of government policies designed to favour domestic companies, especially state-owned enterprises (SOEs), which do appear to clash with the principle of equal treatment for investments. Industrial-development policies can provide preferential access to land and financing<sup>29</sup>, lower duties on imported inputs, and subsidies for research and development<sup>30</sup> to which foreign-invested firms in China might not have access. Indeed, particularly with regard to financing, SOEs in China are thought to enjoy better access even than their counterparts in the domestic private sector. The proliferation of active policy support for sectors like automotives and electronics in the wake of the economic slowdown of 2008-09 raises the concern that support issued under such measures may in practice be restricted, or disproportionately allocated, to domestic enterprises<sup>31</sup>. Policies like the “home appliances to the countryside” programme (subsidising appliances for sale in rural areas), which are based on approved supplier lists, are particularly vulnerable to unequal treatment—though several foreign manufacturers appear on the lists of approved products under this particular policy.

The effect of a BIT on policies designed to favour “national champions” and SOEs will of course depend on the phrasing of the treaty. Some governments have specifically included clauses to protect their ability to maintain policies that favour domestic enterprises. Morocco’s investment treaty with the UK, for example, includes a provision exempting it from providing national treatment in the case of benefits resulting from “government aids reserved for its own nationals in the context of national development programmes and activities”. These sorts of exemptions are not typically included in BITs that China has signed to date, so optimists might hope that a potential BIT’s clauses on national treatment and fair and equal treatment could prove a useful tool in curbing policies that favour SOEs.

However, it is questionable whether a BIT would be able to provide investors with an important tool to fight this discrimination in favour of SOEs and domestic firms. First, the jump between there being a widespread perception of unequal treatment and proving it would be difficult to make (see Transparency and uniformity of regulations below). Second, China has a marked tendency towards aggressive responses when challenged. Countries that impose sanctions on Chinese goods may find themselves

<sup>28</sup> UNCTAD, Latest Developments in Investor-State Dispute Settlement, IIA Monitor No.1, International Investment Agreements, p.6

<sup>29</sup> Economist Intelligence Unit, *China Country Finance* 2009, p.101-102

<sup>30</sup> American Business in China 2009 white paper p.96-98

<sup>31</sup> For additional details on examples of industrial policies under this plan see Economist Intelligence Unit, *China’s stimulus plan*, a six-month report card, p.19-20

facing disproportionately large sanctions in retaliation<sup>32</sup>. Similarly, companies operating within China fear that if they took on the government in a major court case, their business within China would be irretrievably damaged—even if they won.

An extreme example of the Chinese authorities' strong response to companies that are perceived to challenge its interests was provided in 2009, when several executives from Rio Tinto, an international mining giant, were arrested. The incident followed Rio Tinto's rejection of a bid by Chinalco, China's state-owned aluminium giant, to raise its stake in Rio Tinto, as well as Rio Tinto's refusal to accept a reduction in iron-ore contract prices during negotiations with China in 2008-09. Although charges of espionage against the Rio Tinto executives were eventually dropped to bribery, the case clearly attracted political interest at the highest levels.

It is thus quite likely that only a company willing to write off its commercial future (at least in the short- to medium-term) in China would be willing to take advantage of the potential for international arbitration. And given the growing importance of the Chinese market, there are few foreign investors who would fall into this category. Against this background, it is not really a surprise that despite the fact that China has signed the second-largest number of BITs after Germany, it has yet to have a single investment-treaty claim filed against it (as at end-2008)<sup>33</sup>. By contrast, the US government is frequently taken to court (even by its own citizens!), and foreign companies feel little compunction in taking it to court under investment-treaty commitments—12 cases had been filed against it as at end-2008<sup>34</sup>.

The Chinese government would probably resist strongly any efforts to use a BIT as a tool to undermine its ability to favour SOEs and build up national champions. This is partly because it is keen to protect and promote Chinese SOEs for reasons of national pride (see Market access for more discussion). But another important reason for this stance is the government's belief that its influence over these “commanding heights” of the economy is one of its most important tools for managing the economy. It is possible that this situation will change as the country develops and other macroeconomic policy tools—like interest rates—become more effective, but this will probably take many years.

#### **Arbitration and China's existing BITs**

Most bilateral investment treaties allow investors to take disputes with the host state to binding international arbitration under the UN Commission on International Trade Law (Uncitral) Arbitration Rules or the International Centre for Settlement of Investor Disputes (ICSID), although other options exist. The process of arbitration frameworks bypassing national courts is naturally somewhat controversial. Although this allows an level playing field that grants protection to investors in both of the signatory states to a BIT, it simultaneously impinges on the sovereignty of those same states to make subsequent changes to their regulatory environments—or at least increases the cost of making such changes, owing to the need to compensate affected investors. This can reduce states' flexibility to pass laws in response to specific circumstances. Singapore, for example, wished to include provisions in its BIT with the US allowing it to limit

<sup>32</sup> In 2000, for example, China responded to a rise in South Korean tariffs on imports of Chinese garlic by banning imports of South Korean mobile phones and polyethylene.

<sup>33</sup> UNCTAD, Latest Developments in Investor-State Dispute Settlement, IIA Monitor No.1, International Investment Agreements, p.13

<sup>34</sup> Ibid, p.13

short-term investments in emergency circumstances (see p. 40). Some feel that arbitration decisions made under BITs have interpreted the contents of the treaties beyond their original intentions. This could be a growing concern, since BITs are often short and vague relative to other international treaties, allowing leeway for broad interpretation. Others worry that BITs that apply to post-establishment protection of investments may result in governments becoming more cautious about screening the types of investment that they let in.

China's BITs appear to prefer arbitration through the ICSID mechanism. Most investors regard ICSID favourably, thanks to its links with the World Bank—a connection suggesting that failure to comply with an arbitration ruling would result in the unfavourable attention of the World Bank, which might affect its decisions on financing. Allen & Overy<sup>35</sup> note that states that sign up to ICSID resolution (including the US and China) “are not able to challenge awards in their courts and must enforce the pecuniary obligations of awards as if they were a final judgment of their own highest court”. However, the ICSID Convention does not override domestic laws relating to sovereign immunity from execution of awards, and arbitration decisions can be revised or annulled on review. Full proceedings under ICSID often run for two to three years.

There is no known example of a case being brought by an investor against China under a BIT. An important reason for this is likely to be the fear that doing so would imperil an investor's future business prospects in China, although other considerations may be a lack of awareness of the possibility, law firms' reluctance to promote this option and concerns about the reliability of the process. To date, foreign investors seem to have shown a preference for pushing their governments to protect their investments by encouraging China to enforce fully the terms of its WTO accession commitments. Lobbying by US entertainment companies, for example, was a factor behind the US move to bring a case against China under the WTO over the deficiencies in its intellectual-property-rights legal system (a decision, largely against China, was reached in January 2009). Chinese investors, by contrast, have been known to pursue claims under China's BITs. For example, under the terms of the China-Peru BIT, Tsia Yap Shum launched a claim that actions undertaken by Peru's tax authority in 2004 undermined his business.

### Performance requirements

In line with its WTO accession protocols, particularly under the Agreement on Trade-Related Investment Measures (TRIMs), China has already revised many laws relating to performance requirements associated with investment, including those that affect export performance, local-content requirements and technology transfers. By and large, foreign investments are no longer required to adhere to local-content or export-performance requirements before being approved. Nevertheless, this sometimes may unofficially be a factor in officials granting approval<sup>36</sup>. This is partly because foreign investors are free to sign up informally to such commitments. (It is possible that contracts with such “voluntary” clauses could be challenged under WTO auspices, but as noted above few foreign companies are willing to face the repercussions of bringing legal cases against the authorities in China.) The range of performance requirements banned under US BITs can be wider than that secured under the TRIMs agreement,

<sup>35</sup> See <http://www.allenoverly.com/AOWeb/binaries/51290.pdf>

<sup>36</sup> Confidential interviews conducted by the Economist Intelligence Unit.

but in practice problems in China today seem related more to the poor implementation of existing protection.

An increasing number of foreign investors in China are aware of growing pressure to transfer technology to their China-based vehicles. Given the high degree of discretion Chinese officials enjoy in approving foreign investments, many businesses feel that encouragement of such transfers in practice often amounts to requirement. The 2009 American Chamber of Commerce's white paper notes that "China has long made technology transfer a requirement of approvals for investments and sales in support of large-scale projects, particularly for those that are publicly funded"<sup>37</sup>. Its point is re-emphasised by the European Chamber of Commerce's position paper, which adds that the authorities can sometimes require companies to provide highly confidential information for product or plant approval. Indeed, the experts who look at this information to evaluate the approval sometimes also work for, or have links with, competitors of the foreign companies concerned, leading to leakage of technology<sup>38</sup>. In some sectors, foreign investors are required to have proprietary technology. In sectors like steel where this condition is complemented by caps that limit foreign companies to minority stakes, this arguably would result in an effective requirement for the transfer of technology<sup>39</sup>.

A BIT that clearly ruled out making investments conditional upon technology transfers might give individual companies an extra avenue for pursuing claims against the Chinese government when these became an issue (although as mentioned earlier, whether they would wish to challenge the government like this is another matter). However, a BIT would be unlikely to influence policies that promote technology in investments without discrimination between foreign and local companies—such as the granting of tax incentives to companies whose investments held desirable or high-technology intellectual property. Given the existing protection that the TRIMs agreement should offer, the problem lies at least in part in the flexibility that local officials have—unofficially—in approving or denying investments. Proving under a BIT that such behaviour was discriminatory would be tough (see Transparency and uniformity of regulations below).

### Capital flows

In theory, there is not a big gap between the standard US and Chinese BITs regarding payments on transfers related to investments and returns, despite the complication of China's capital-account restrictions. China already allows businesses to repatriate profits and make other legitimate business-related payments. Nevertheless, foreign investors in China have raised concerns over the Chinese government's monitoring of capital flows. Transfer-pricing arrangements and royalty payments can come under particular scrutiny, causing delays and regulatory hassle for businesses. Questions on royalty payments in particular may sometimes be designed to encourage companies to transfer technology into China-invested enterprises. It remains questionable whether standard BITs would be able to offer much additional support for free transfers of funds by foreign-invested companies.

<sup>37</sup> American Business in China 2009 white paper, p.18.

<sup>38</sup> 2009/10 European Chamber of Commerce in China Position Paper, p.77

<sup>39</sup> Terence P Stewart, US-China Economic and Security Review Commission testimony, p.5. Accessed at [http://www.uscc.gov/hearings/2009hearings/written\\_testimonies/09\\_03\\_24\\_wrts/09\\_03\\_24\\_stewart\\_statement.pdf](http://www.uscc.gov/hearings/2009hearings/written_testimonies/09_03_24_wrts/09_03_24_stewart_statement.pdf)

Meanwhile, China has some concern about the additional limitation that a BIT might impose on that country's ability to impose restrictions on financial transfers during times of economic crisis. The government is keen to maintain an ability to prevent both potentially destabilising inflows of speculative capital and sudden outflows of funds. The memory of the impact that volatile financial flows had during the Asian financial crisis of 1997-98 looms large, and such fears would probably have to be assuaged if a BIT were to be successfully concluded. The recently concluded China-Mexico BIT, for example, includes an exemption permitting the temporary imposition of controls on currency convertibility if threats emerge to the balance of payments<sup>40</sup>. With regard to system-destabilising outflows, Article 20 of the US model BIT might potentially provide the basis for permitting special-case restrictions (especially if applied equally to Chinese and US institutions). However, the sensitivity of limiting transfer flows is highlighted by the fact that the US rebuffed Singapore's efforts to include a special exemption in their bilateral FTA allowing Singapore to limit short-term investment activities in exceptional circumstances<sup>41</sup>.

### **Transparency and uniformity of regulations**

China suffers from an immature and unsatisfactory regulatory regime, despite substantial improvements over the last few decades, which would pose problems for implementing a high-quality BIT. Foreign investors are concerned at the lack of consultation that often precedes new regulations, especially at the local level in many parts of China. The recent agreement under the Strategic Economic Dialogue (now Strategic and Economic Dialogue) to allow all draft regulations affecting business to be released for a one-month commentary period is welcome in this regard, but it appears it is only being implemented with patchy effectiveness<sup>42</sup>.

When it comes, legislation is often vague and the implementation of regulations within China is usually a matter for local authorities, leading to a high degree of discretion in enforcement and thus widely varying practices in terms of implementation across different regions. Clarifying regulations sometimes come out long after the laws to which they apply, and the laws themselves are often changed with unnerving frequency. The lack of reliable and consistent enforcement of laws is of particular relevance to the aspects of a BIT dealing with national-treatment and most-favoured-nation status. Discrimination favouring local companies would be especially hard to prevent if courts do not enforce regulations strictly and consistently. (Courts in China are subordinate to regional governments, whose local officials may have commercial or other interests in Chinese companies within their jurisdictions.)

Theoretically, regional governments do fall under the coverage of a BIT. A state is generally held to be liable for the actions of lesser entities such as "provincial or regional authorities, the security services and police, courts of law and other judicial or quasi-judicial institutions, private companies working on behalf of the State, public-sector utilities, corporations over which the State exercises *de facto* control and individuals working for or on behalf of the State"<sup>43</sup>. This is the case even if the state in

<sup>40</sup>Source can be accessed at <http://finance.jrj.com.cn/2008/12/0104392922830.shtml>.

<sup>41</sup> Ibid. In the Singapore case, the US did allow some exemptions—for example that if the restrictions imposed lasted less than a year and caused no realised loss for an investor, Singapore would not have to provide compensation.

<sup>42</sup> 2009/10 European Chamber of Commerce in China Position Paper, p.11

<sup>43</sup> Watson, Farley & Williams, Introduction to investment treaties,



practise has little control over these entities. Past experience shows that investors have brought cases under investment treaties based on actions at the sub-national level. A Congressional Research Service report has noted that under NAFTA, “investor-state provisions gave rise to numerous ‘indirect expropriation’ claims against sub-national (state) governments in the United States, Mexico and Canada over environmental and other regulations”<sup>44</sup>.

Nevertheless, if an investor wished to bring a case to international tribunal under a Sino-US BIT, proving discrimination might be difficult. The government’s position may, at face value, be consistent with non-discriminatory treatment, making it hard to prove a breach<sup>45</sup>. In addition, discriminatory policies may sometimes not be explicitly spelt out, either at the local or at the national level, but may still exist as an understanding. The lack of transparency about inner government policy and workings would be a further impediment to proving a case. It is unlikely the government would willingly surrender documentary evidence during an investigation into whether discriminatory treatment was policy, especially if it was incriminatory. Indeed, many relevant documents would doubtless be considered state secrets. Contradictions between policies and statements issued by various public officials at different levels of authority (which occur frequently) would create further challenges in determining whether or not a policy was officially “sanctioned”.

In principle, a BIT could improve the lack of transparency by including clauses to address this issue. Although these are not standard in Chinese BITs, they have appeared in ones signed by the United States. Nevertheless, the fact that China has repeatedly committed to improving transparency in past agreements and yet has still fallen short of successfully implementing these conditions suggests that hopes on this front should be contained.

### **Market access**

There is a perception among many foreign investors that China is tightening access to its markets as far as investments are concerned. This is particularly true for mergers and acquisitions (M&A). New regulations were issued in 2006 that allowed a further government-approval step for M&A deals that affect “national economic security” or that involve famous Chinese brands<sup>46</sup>. The implementation of the anti-monopoly law (AML) in 2008 further toughened the situation. The vague definitions in these regulations give broad scope for rejecting deals. Many observers think that these measures may sometimes be used to shield monopolistic or incumbent Chinese enterprises against competition from foreign-invested enterprises. Many observers also viewed the rejection of Coca Cola’s bid for Huiyuan, a Chinese juice producer, in 2009 over monopoly concerns as highlighting the government’s wish to preserve “national champions”. According to this argument, Huiyuan was simply too big for officials to allow it to be taken over by a foreign company<sup>47</sup>.

Meanwhile, the government continues to adjust the foreign investment catalogue in accordance with its policy goal of encouraging foreign investment in sectors that help

<sup>44</sup> CRS report for Congress on the proposed US-Panama Free-Trade Agreement, updated July 3rd 2007, p.17. The report adds that none of the claims against the US prevailed in these cases, however.

<sup>45</sup> Interview with Erin Ennis

<sup>46</sup> Kenneth Davies, OECD Observer, [http://www.oecdobserver.org/news/fullstory.php/aid/2138/China\\_s\\_investment\\_watch.html](http://www.oecdobserver.org/news/fullstory.php/aid/2138/China_s_investment_watch.html)

<sup>47</sup> See, for example, lawyer Dan Harris of Harris & Moure, <http://www.amchamchina.org/article/4455>

China's move up the economic value chain and away from polluting or low-value-added industries. In the long run, this may close off more sectors to foreign investment.

Against this background, some advocates of a BIT view it as a "new WTO" agreement—that is, a way of encouraging China to open its market and allow foreign direct investment (FDI) into new sectors. Traditional US BITs include a pre-establishment protection element, which in China's case would prevent it from discriminating between Chinese and US investors in reviewing and authorising investments, granting business licences and other steps necessary to set up an investment. Clearly, the scope of businesses that local companies are permitted to undertake is much wider than that open to foreign companies, so this would mark a major reform. Among the sectors that could benefit are automotives, petrochemicals, information, telecommunications and technology (IT&T), and certain renewable energy industries; in all these sectors, foreign investment is restricted to joint ventures in which the level of foreign shares is capped. Financial services would also face less discriminatory treatment at the establishment phase (for example, discriminatory capital requirements now deter foreign banks from expanding branch networks). Although this would clearly be extremely beneficial if it could be achieved, the outlook for improving market access through a BIT is difficult at best. Traditionally, China's BITs deal only with the post-establishment phase of an investment.

Negotiators for other OECD nations that have recently signed bilateral economic treaties with China report that their opposite numbers have been extremely unwilling to countenance any liberalisation of restrictions on foreign investments<sup>48</sup>. Indeed, most Chinese officials suggest that there is still lingering resentment over the concessions offered under the WTO accession. In practical terms, the fact that state-owned enterprises (SOEs) dominate many of the industries that remain closed or restricted would further impede liberalisation; moreover, the leaders of the SOEs have a powerful lobby in government, and often their political rank is equivalent to ministerial status. Potential critics of a BIT would probably argue that adjusting the present investment-approval regime to adapt it to the US model BIT would not only affect areas the Chinese government sees as important for security reasons but would also affect the government's ability to control sectors that are important for economic planning—such as housing<sup>49</sup>. It would require a very senior advocate of further opening within the government, possibly a vice-premier or higher, to campaign actively in favour of change in order to press it forward. At present, it is hard to discern such a figure.

### Chinese interests

If China were to be persuaded to back a pre-establishment clause in a BIT, it would probably have to be offered some form of concessions on the approval process for Chinese companies entering the US market. There is a perception within China that the US may use spurious (in Chinese eyes) claims about strategic threats to block Chinese investments, notably through the CFIUS review process. Strong political pressures to block attempted Chinese investments in US companies have certainly

<sup>48</sup> Confidential interviews conducted by the Economist Intelligence Unit.

<sup>49</sup> accessed at <http://finance.jrj.com.cn/2008/12/0104392922830.shtml>. Tian Feng notes that measures to control economically important sectors do not necessarily need to discriminate between local and foreign companies, but notes that liberalisation of investment restrictions would likely be a "one-way street".

been felt in high-profile cases, such as the bid by China National Offshore Oil Corp (CNOOC) for Unocal and Huawei's attempt to purchase an interest in 3Com. Concessions on the CFIUS approval process might win Chinese flexibility for making greater concessions, especially as Chinese companies look to expand within the US. (The winding down of the US government's stakes in major corporations in the financial and other sectors will probably prompt intense interest among Chinese companies keen to expand abroad.) However, the reality is that the Foreign Investment and National Security Act recently strengthened CFIUS processes; hence, it is unlikely that they would be up for negotiation.

Chinese companies are in any case expanding their presence in the US and would probably see value in other aspects of a BIT, such as those requiring national-treatment and most-favoured-nation status. One particular area that might interest them would be that allowing special consideration of investors engaged in activities associated with investments when it comes to visas and working permits; the difficulty in obtaining visas to visit and work in the US is a source of much irritation for Chinese businessmen. Nevertheless, the advantages these areas offer to Chinese firms would be unlikely to persuade China to move away from its traditional post-establishment model of protection for investments. Moreover, some Chinese academics argue that "a BIT's role in encouraging Chinese enterprises to 'go out' would be limited", owing to the significant gap between Chinese firms' technical and management capacities, relative to those in the US, which manifest as low rates of return on investments in the US<sup>50</sup>. Low returns are especially damaging for prospective Chinese investments in the US, as the expected trend of renminbi appreciation against the US dollar in the next few years will further reduce the prospective profit in renminbi terms.

One more crucial point for the Chinese is the protection of the value of its investments in US securities. Acquisitions of US-issued debt represent the most important path at present for Chinese investment capital to enter the US<sup>51</sup>, and US-government debt is the most important element within those acquisitions. According to figures from the US Treasury, mainland Chinese investors were the largest holders of US Treasury securities in October 2009, with holdings worth US\$798.9bn<sup>52</sup>. Although it is difficult to differentiate between private and public holders, it is likely that a very large chunk of this total reflects the country's foreign-exchange reserves, which were valued at US\$2.3trn at end-September 2009<sup>53</sup>. Indeed, it is possible that China's actual holdings of US debt may be even higher, if they are held indirectly via financial institutions in third-party countries. Preserving the value of China's investments in these instruments has become an important policy prerogative for the Chinese government<sup>54</sup>.

Theoretically, a BIT could also serve to boost inward US investment in China. A Chinese researcher, Tian Feng, has pointed out that US direct investment in China is relatively low, both as a proportion of total outbound US direct investment and as a

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<sup>50</sup> Ibid.

<sup>51</sup> accessed at <http://finance.jrj.com.cn/2008/12/0104392922830.shtml>

<sup>52</sup> <http://www.treas.gov/tic/mfh.txt>

<sup>53</sup> IMF, via Haver Analytics.

<sup>54</sup> See, for example, comments made by China's premier, Wen Jiabao, quoted in the New York Times, <http://www.nytimes.com/2009/03/14/business/worldbusiness/14china.html>

proportion of China's received inward direct investment. Nevertheless, she cautions that the role of BITs in stimulating inward investment is far from clear and that additional uncertainty is raised by the question of the potential US "pre-establishment" BIT model, which is less researched than the more commonly used "post-establishment" model. In addition, US investment in China has only recently picked up, despite the reforms associated with, for example, China's 2001 entry into the WTO. Indeed, entry into the WTO saw much-more-important and wide-ranging reforms than BITs tend to bring about. As a result, it is not clear how much benefit a BIT would have in stimulating US investment in China<sup>55</sup>.

**Impact** As US Treasury officials have noted, the most significant impact of a BIT would be that it would "send a powerful signal that our two countries (the US and China) are committed to open investment and to treating each others' investors in an open and transparent manner"<sup>56</sup>. Indeed, economic officials from other nations that have negotiated BITs have also highlighted the reassurance they can provide—for example, against the risk of expropriation—as one of their strongest advantages for businesses.

Depending on the quality and details of the Sino-US BIT, it could also have a much more tangible and valuable effect. Advocates of an agreement look to the model of China's WTO entry, which was a catalyst for the country's legal development, vastly improving the regulatory environment for foreign businesses. If the more optimistic hopes were realised regarding a BIT's potential market-access concessions, this would open up opportunities for US businesses that could be worth several billion US dollars or more, depending on the extent of the concessions. But even if a BIT served merely to push China to make its regulatory environment more transparent, and to implement its laws more effectively and in a fair and equal manner, foreign companies would welcome it. By contrast, although improvements in the regulatory environment will not depend on cases being brought under a BIT, it is likely that the continued failure of companies (or governments) to bring cases against China under a future BIT or existing economic treaties would diminish the impact of any deal agreed.

Some would argue that the mere process of highlighting problems through negotiating a BIT will have an effect in forcing the Chinese authorities to focus attention upon the flaws within their regulatory regime for business. For the BIT to have a positive effect, China does not need to travel the full distance towards global best standards. Realistically, this may still be beyond its capacity, given its developing-country status and political system. But continued progress in this direction would be a beneficial result in and of itself, especially given present fears that China's leaders may be backsliding away from commitments to economic openness.

Meanwhile, on the Chinese side, the BIT negotiations allow a way for the Chinese government to engage in discussions over the challenges their countries' enterprises face investing in the US. Given the potential impact that Chinese investments could have in terms of job creation and the development of a more balanced economic relationship between the two countries, this would be a welcome development. Nevertheless, given that Chinese companies in the US already enjoy relatively strong regulatory protection (notably in terms of fair and equal treatment), the effect of a

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accessed at <http://finance.jrj.com.cn/2008/12/0104392922830.shtml>

<sup>56</sup> <http://www.ustreas.gov/press/releases/reports/sedusfactsheet.pdf>, p.2

successfully concluded BIT for them would probably be less significant than for US companies in China.

A final impact worth noting is the broader international significance that a US-China BIT would have. As a major treaty between the world's largest economy and the third-largest one, it would probably serve as a model for future BITs, particularly when both countries negotiate bilateral deals with other economic partners. Meanwhile, since many countries have BITs with China and the US that contain most-favoured-nation clauses, the benefits of a Sino-US BIT could percolate down to companies from these other locations. As this increases competition, such regulatory changes should boost productivity and encourage job-creating investment within both China and the US.

## Conclusion

A Sino-US BIT would provide significant legal support for US companies in a number of fields. It would strengthen their claims to non-discriminatory treatment and bolster their right to produce without performance requirements or restrictions on their ability to transfer funds into and out of their investments. At a time when China appears to be retreating in some aspects of its welcoming attitude towards foreign direct investment (FDI), the extra security a BIT could offer to investors would be welcome.

Nevertheless, for an investor to prove a case in international arbitration against China under the terms of the BIT would be difficult, given the existing complexities and grey areas within the Chinese legal and political system. Another problem would be the fact that any foreign investor challenging the Chinese government would also expect to face retribution that might shut them out of the rapidly growing local market. (This may also be a factor explaining why no cases have yet been brought against China under a BIT, despite the many such treaties that it has signed.)

If China could be persuaded to adopt a pre-establishment BIT model as part of negotiations with the United States, this would represent a major breakthrough, and would offer US companies substantially greater access to the Chinese market in terms of investment opportunities. However, the US would face difficulty in offering reciprocal moves to liberalise access to its own market in terms of investment, especially given the recent strengthening of the CFIUS review process. As a result, it is hard to envisage the Chinese moving towards a pre-establishment model.

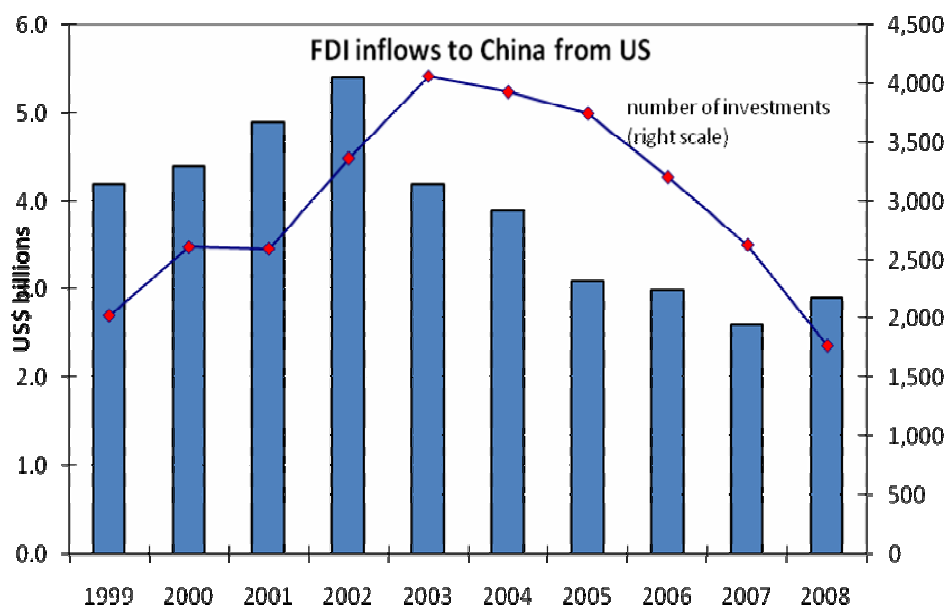
## V. Implications for the US economy

### Overview

Successful conclusion of a BIT between the US and China—in addition to being an economic achievement—would represent an important political accomplishment, particularly in light of the rifts created by two failed high-profile attempts in the past several years by China to invest in the US. Severe opposition by US lawmakers, on national-security grounds, caused the failures of an US\$18.5bn bid by China National

Offshore Oil Corp (CNOOC) to buy Unocal in 2005 and a US\$2.2bn offer by Huawei Technologies, in partnership with Bain Capital Partners (a US-based private-equity firm) to acquire 3Com. Indeed, the issue of the fairness of US authorities' regulatory oversight of potential Chinese investments is an area of great concern for China in the BIT negotiations.

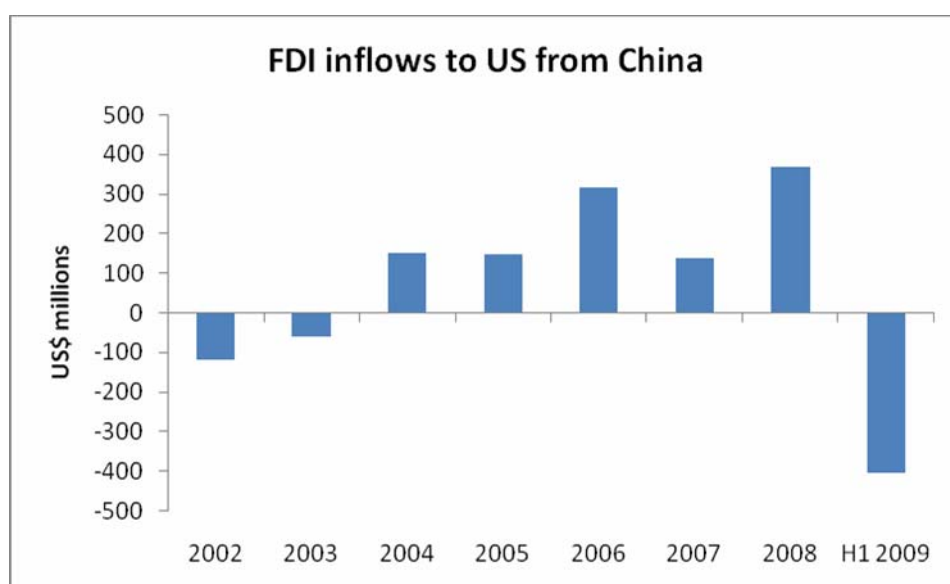
The value of inflows of foreign direct investment (FDI) from the US to China has ebbed and flowed over the past decade, but generally declined since reaching a peak of US\$5.4bn in 2002. Likewise, the number of US investments in China has declined every year since 2003. A small uptick in 2008—to US\$2.9bn, from US\$2.6bn in 2007—is likely to be followed by a steep decline in 2009, as a result of the global economic crisis that took hold in late 2008.



Source: Ministry of Commerce (MOFCOM), China.

Note: Dollar figures on left scale represent non-financial, utilised FDI.

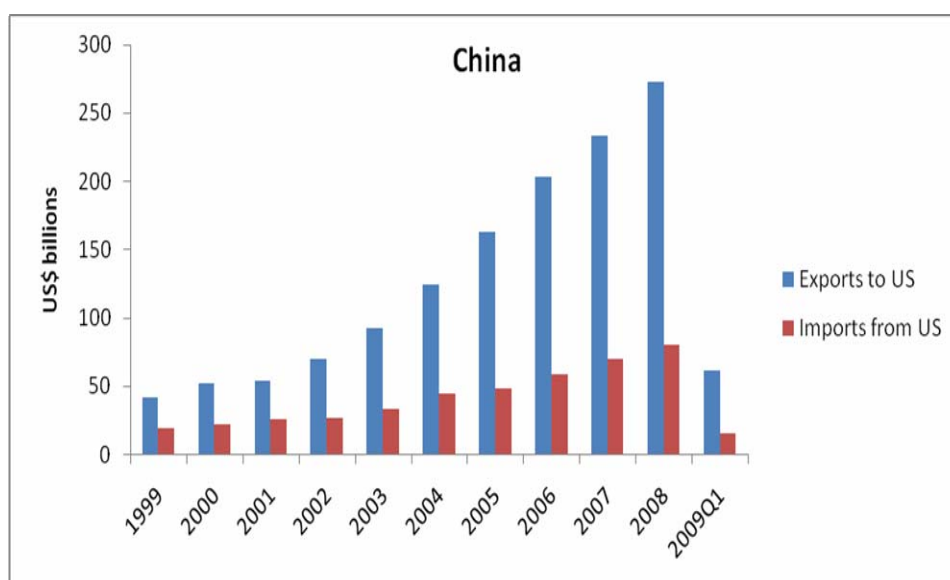
The value of China's inflows of foreign direct investment (FDI) to the United States has also fluctuated in recent years. In general, though, the scale of FDI flows from China to the US is significantly smaller than flows from the US to China (likewise, aggregate FDI inflows from the world to the US reached US\$316bn in 2008, whereas inflows to China were US\$108bn). The high in recent years of US\$368m China-to-US FDI, reached in 2008, is surely to be followed by a decade low in 2009. Indeed, the first half of 2009 saw a bilateral outflow of FDI of US\$407m, as Chinese companies concentrated on domestic business in the face of economic downturn.



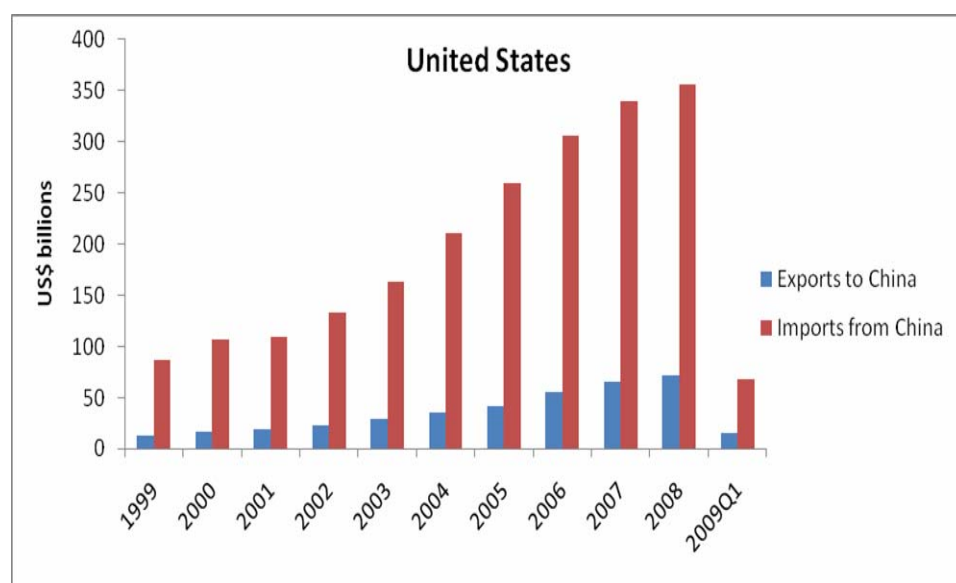
Source: US Bureau of Economic Analysis.

Note: Figures are not seasonally adjusted; negative figures indicate outflows of FDI. Data for 2009 is estimated. Data for FDI inflows from China for years prior to 2002 are not available.

In contrast to FDI flows, trade flows between the US and China steadily increased in 1999–2008, from both an export and import perspective. According to data from the International Monetary Fund, China edged out Canada in 2007 and 2008 as the country from which the US imports the most. Though data reported by the two countries (compare the graphs) shows some variation in data, the general pattern is that China exports much more to the US than it imports from it—and vice versa for US trade with China. And although both countries reported a pullback in trade flows during the first quarter of 2009 (with imports more affected than exports), recently released US import estimates for July 2009 show the fastest monthly increase since the Commerce Department began publishing the data in 1992. That increase is one indication that the US is emerging from recession.



Source: IMF Direction of Trade Statistics database. Data for 2009 are estimated.



Source: IMF Direction of Trade Statistics database. Data for 2009 are estimated.

## Extent of reciprocal market access

Under the model US BIT text, the partner country receives “treatment no less favourable” than domestic investors from establishment through to sale or disposition of the investment. By several accounts, though, China is unlikely to sign the model agreement, thus leaving open the door to negotiation in terms of how much the treaty would diverge from US BITs with other countries in terms of market access. Both the US and China are moving somewhat slowly and cautiously in proceedings, as this BIT will surely be the most difficult one either country has worked out.

Specific market-access concerns from the US side include regulatory barriers and delays, lack of transparency, discriminatory treatment of US businesses at the provincial and local levels, local-content requirements and capital controls. By some accounts, the US will also pursue pre-establishment guarantees—that is, guarantees against discrimination before an investment is established. China is likely to fight for guarantees only after establishment. In addition, the issue of the treatment of China’s state-owned enterprises by the Chinese government will probably continue to be on the negotiating table going forward.

## Economic sectors most likely to be affected

It is difficult to predict which business sectors a US-China BIT would most affect, in large part because of the way the US model BIT approaches market access. Barring dramatic changes to the 2004 model text, the revision of which is now underway, it is likely that the new model text will afford investors in future US BIT partner countries similar national treatment as the current text—that is, treatment no less favourable than it accords investors from the US (as contained in Article 3 of the 2004 model BIT). That said, US BITs contain exceptions to national treatment for certain sensitive sectors. These are spelled out in an annex to each BIT in what is sometimes referred to



as a “negative list”, where the US and the partner country list, separately, which of their sectors are subject to exceptions from national treatment. Use of such exceptions may be a sticking point in the US-China BIT negotiations.

When the US uses a negative list, the partner country is allowed to invest freely in all sectors of the US economy except the ones on the list, which may not be completely off limits to the partner country’s investors but are accorded something less than standard national treatment. China’s BITs, however, have traditionally addressed the issue of national treatment from a more vague perspective, simply stating that foreign investors are subject to domestic Chinese laws and leaving investors to navigate a sometimes tricky path in determining what those laws are.

Negative lists enumerated by the US in BITs over the past decade have typically included air transport, banking, cable television, energy/power production, insurance, ownership of real property, radio/satellite communications and telephone/telegraph services. Though this list of sector exceptions is not standard across US BITs, it is difficult to imagine that any of those enumerated here would not be excluded in a BIT with China.

Certain types of natural resources may also be included in the US’s negative list in a US-China BIT. Recent CFIUS reviews have not been supportive of such investments by China. As at mid-December 2009, for example, CFIUS is expected to recommend that President Obama reject the proposed purchase by a Chinese company of a 51% stake in Firstgold, a gold-mining company with properties in Nevada. The publicly-stated rationale for the expected decision centres on the fact that Firstgold’s properties lie some 50 miles from a naval air station and that the transaction might result in sensitive military technology being passed on to foreign governments. Opponents of the recommendation counter that China’s growing ownership of the world’s supply of precious metals is a factor in the decision.<sup>57</sup>

Despite the probable limitations on some sectors, a fairly broad swath of the US business community voiced its support for the US-China BIT directly to President Bush at the start of treaty negotiations in 2008. The industry associations supporting the BIT include those representing apparel and footwear, electronics, equipment manufacturers, insurance, financial services, information technology, retail and textiles.<sup>58</sup>

According to one person interviewed for this analysis, a US-China BIT may contain provisions that would improve prospects for Chinese investment in the United States at a state and local level. That same person expressed hope that a US-China BIT would lead to better investment conditions for his industry, insurance.

## Macroeconomic impacts

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<sup>57</sup> List of typical US negative-list elements taken from analysis of individual BITs, available at [http://tcc.export.gov/Trade\\_Agreements/Bilateral\\_Investment\\_Treaties/index.asp](http://tcc.export.gov/Trade_Agreements/Bilateral_Investment_Treaties/index.asp).

<sup>58</sup> Information in this paragraph from a public letter to President Bush in July 2008; original text in accompanying PDF.

Although a US-China BIT would not create a completely transparent Chinese investment environment, it would serve as a solid improvement in terms of protection for US investors in China, particularly in terms of strengthening rule of law and market-directed reforms. These outcomes, along with likely increased inflows of US foreign direct investment (FDI) into China and greater assurances from the US side that future Chinese investments will be evaluated in a non-discriminatory manner, would be among the most important effects of a successful US-China BIT.

## VI. Interviews

To complete this study, the Economist Intelligence Unit conducted interviews with the following officials and organisations:

1. American Insurance Industry Association
2. A former official of the George W. Bush Administration who represented the US in Strategic Economic Dialogue discussions
3. Erin Ennis, US China Business Council (USCBC), Washington, DC
4. American Chamber of Commerce in Beijing
5. Robert Stumberg, Professor of Law and Director, Harrison Institute of Public Law, Georgetown University
6. Thea Lee, Policy Director, AFL-CIO

Summary transcripts of interviewees or organisations who agreed to have their remarks on record are presented in the following pages.

### 1. American Insurance Association representative

#### **What are the insurance industry's major concerns vis-à-vis the US-China BIT negotiations?**

The most significant problem facing the US insurance industry in China is high regulatory barriers. At present, foreign companies represent less than 2% of the property-and-casualty insurance market in China, a percentage that would be significantly higher if they were not being held back by Chinese regulation. The principal concern is that companies may not expand geographically unless they complete extensive application procedures on a province-by-province basis. Insurance companies are also shut out of certain product lines, namely third-party automobile liability insurance.

Commitments concerning the insurance industry that China made as part of its WTO accession in 2001—in particular its agreement to grant licences to more foreign companies—represented a new plateau in terms of its overall regulatory environment; in practice WTO accession has not done much to improve the business environment for insurance companies. The China Insurance Regulatory Commission continues to be a major hindrance to doing business. The insurance industry views the BIT as an

opportunity to push China to a higher plateau in terms of openness and less-restrictive regulation (that is, creating a better business environment for insurance companies).

**Is there enough demand for insurance in China to absorb a significantly larger US insurance presence?**

Without a doubt, yes. The rapid increase in car ownership, in particular, presents a prime opportunity for insurance companies. An expanded insurance market presence would also have a positive impact in terms of protecting people from natural disasters. During the Sichuan earthquake in 2008, for example, buildings that one US insurance company had advised on sustained only very minor damage, while structures around them crumbled.

Insurance is on the “negative list” (meaning that investment in the sector is restricted) in the text of many US BITs.

**What is the likelihood that insurance will be on the negative list in the potential US-China BIT, and what does that mean for the US insurance industry in China?**

Though the interviewee did not want to predict whether insurance would be on a potential list of industries subject to limitations under the BIT, he believes it would be “amazing” if China agreed to the model BIT text.

**What would be the impact of an expanded US insurance-industry presence in China on other industries?**

From the perspective of the financial industry, at least, a rising tide would lift all boats—that is, growth of one subsector of the industry would benefit other subsectors.

**What larger impacts (macroeconomic or otherwise) would an active US-China BIT have?**

Regardless of the outcome of the US-China BIT negotiations, it is certain that serious negotiations on investment and trade are a good thing for both parties, as it encourages mutual openness to foreign investment (particularly on China’s part). A BIT “with teeth” would be an even greater achievement. Furthermore, the BIT negotiations will set the stage for future open discussion of trade and investment issues.

## **2. A former official of the George W. Bush Administration who represented the US in Strategic Economic Dialogue discussions with China**

**What are the issues of greatest concern for the US and China within the BIT negotiations?**

It is important to keep in mind that past attempts at US-China BIT negotiations foundered due to China’s refusal to agree to stipulations providing for expropriation protection, fair and equitable treatment, and the ability of an investor to initiate third-party arbitration. In recent BITs, however—with Germany, Finland and other countries—China has agreed to provide such protections.

The real issue in regard to the US-China negotiations with the US is whether China will want to grandfather non-conforming measures from the past or whether it will

move closer to the US approach to BITs, which, according to the interviewee, supports transparency and predictability for investors.

**What are the prospects for reciprocal market access within the framework of a US-China BIT (that is, use of a “negative list” by the US compared with a possible “positive list” by China)?**

Past BITs to which China has been party have simply stated that investment by the partner country is open to all sectors according to domestic laws, a situation that leaves foreign investors to figure out what those laws are. The US approach, however, has been to use a “negative list” (within an annex to a BIT) to identify which sectors are subject to restrictions by each party to the treaty. Though the interviewee did not know how the issue would play out in the context of the current negotiations, he did indicate that China’s vague approach would not be acceptable to the US.

**The issue of how the US financial-services industry would be affected by a US-China BIT has been a topic of discussion during our work on this analysis. Could you speak to the potential impacts of a BIT on financial-services firms?**

The question of how financial services will be affected is wrapped up in the general issue of national treatment—that is, whether China will agree to offer investors establishment and post-establishment protection (as the US accords to partner countries in all of its BITs), or whether it will attempt to impose exceptions. China’s position on this issue remains to be seen. In either case, national treatment of investment will be cross cutting—it will apply to all investors, financial services or otherwise, unless the sector is specifically addressed in an annex [or, presumably, in some equivalent of an annex if the model US BIT text is not the base from which the US-China BIT is developed]. In terms of whether a US-China BIT would improve market access for financial-services companies based in the US, the interviewee’s reaction was only if China agrees to provide adequate establishment and post-establishment protection.

**Do you think the BIT will contain specific provisions for the financial-services sector?**

Yes, but the BIT is all encompassing—that is, financial services should not be more or less affected than other sectors. The bottom line is that if China is willing to open a sector, it is willing to open a sector—and a BIT will not strongly affect that.

**Has the US-China BIT negotiation process changed since President Obama took office?**

Not as far as the interviewee knows—both sides are proceeding with due caution, as they were at the start of negotiations under the Bush administration.

### **3. Erin Ennis with the US China Business Council (USCBC), Washington, DC**

**What is the status of the US China BIT discussions?**

The Obama administration is currently conducting an overall review of the BIT programme, so things are a bit in flux at the moment (Interview conducted in August 2009).

A high-standard BIT would provide added certainty for investors in the market place. If rights were denied, then they [US companies] would have legal recourse.

**Six key elements of a high-quality BIT would include:**

**Non-discrimination requirement.** National treatment and most-favoured-nation (MFN) status.

**International law protection.** Fair treatment compared to local investors.

**Prompt compensation for either direct or indirect expropriation.** Indirect might be related to clean energy—for example, if China were to expropriate clean technology to resolve a climate “emergency” in the same way that Thailand, for example, forced medical companies to hand over drugs.

**Capital flows allowed in and out freely.**

**Removal of performance requirements.** Examples would be the use of local vendors or the export of a certain proportion of product.

**Allowance of arbitration** if investors wish to challenge the government.

A BIT could help “establish a record as to how to attack laws or unofficial practices that are creating an unlevel playing field. It would provide new avenues and new authority for companies to address these issues.”

**The Chinese government has recently been adopting policies that are seen as more demanding of foreign investors, for example, by passing the anti-monopoly law and requiring more technology transfers for tax incentives. How would a BIT affect these?**

Tax status is obviously a big area for technology requirements, but this is not necessarily discriminating (for example, if both domestic and foreign companies are held to the same standards). [And a BIT would not necessarily affect this.]

The anti-monopoly law has a provision for compulsory licensing. There is some concern that this may be used if prices are not low enough—for example, in a field like telecommunications where the Chinese government feels a foreign company is abusing its “monopoly” position.

A “BIT’s value is that it doesn’t try to lay down every situation, but provides some broad principles.”

**How much extra protection would a BIT provide over the existing provisions within WTO-related protocols for issues like technology transfer, export/local-sourcing requirements and transparency?**

The US model BIT prohibits the imposition of performance requirements—such as technology transfer, local-content or export requirements—as a condition for an investment. On transparency, the US model requires that laws, regulations, procedures and administrative rulings related to any matter covered by the BIT be “promptly published or otherwise made publicly available.”

So the BIT would definitely provide additional protection for investors, yet enforcement is key. Under a BIT, investor-state dispute settlement is not the only recourse; government to government would still be an option. And as with any issue, companies would likely seek alternative means to resolve problems before bringing a

case under the BIT, but they would have the additional option of bringing a case to an independent arbitration panel.

### **What will be the problem with enforcing equitable treatment for US companies in China?**

“There’s no doubt it’s going to be difficult to find it [proof of discriminatory treatment]”

For example whether domestic software is being favoured over foreign software in purchases by SOEs. Officials can publicly deny they have a policy of discrimination, but still send a message that means that this happens in practice.

### **What do the Chinese want out of the BIT?**

Chinese firms have a lot of investments in the US and a sense they’re being discriminated against, for example, in US reviews of foreign acquisitions of domestic companies with security ramifications, such as 3Com.

The majority of CFIUS reviews go forward under the radar. It may not be very transparent, but they are relatively fair.

The reality is that the CFIUS review process is not going to be put on the table for negotiation since it has only recently been reviewed and adjusted.

There are many Chinese investments at the state and local level, such as greenfield investments in Texas and Georgia. These might benefit from the provisions of a BIT.

### **What implications would a BIT have for SEC approval of investments?**

I think, in general, the SEC doesn’t need to approve Chinese investments, but the US does reserve the right to restrict investment in some aspects of financial services. There are certain sectors that require regulatory approval for foreign investment over specific levels —say, for instance, banking or broadcast licences. Those areas would be specifically spelled out in the annex to a BIT, since the US uses a negative-list approach.

So, for instance, in the US-Jordan BIT, the US lists these sectors as the ones in which it reserves the right to restrict foreign investment: atomic energy; customhouse brokers; licences for broadcast, common carrier or aeronautical radio stations; COMSAT; subsidies or grants, including government-supported loans, guarantees and insurance; state and local measures exempt from Article 1102 of the North American Free-Trade Agreement (NAFTA) pursuant to Article 1108 thereof; landing of submarine cables; fisheries; air and maritime transport, and related activities; banking, insurance, securities and other financial services; and minerals leases on government land.

### **Would a BIT still be valuable if it diverged from the US-model BIT?**

If the ultimate BIT looked like the US model BIT, regulatory processes would be greatly simplified.

Every Chinese BIT to date has used a positive list and not a negative list, but a negative list (advocated by the US) opens up the potential for new investment fields as they emerge, so it is more liberalising. A more open investment list would provide competition that would help Chinese companies become stronger.

**4. Robert Stumberg, Professor of Law and Director, Harrison Institute of Public Law, Georgetown University, Washington, DC****Are the US-China BIT negotiations materially different from US BIT negotiations with other countries?**

In general, no. But a potential BIT with China is more concerning than other BITs—not because China is expected to act deviously, but because China is such a big economy.

**Could you discuss how the Harrison Institute is involved in the BIT negotiations?**

Clients of the institute are, for the most part, state and local governments that are supportive of international trade but are worried that US trade negotiations are not supporting them. They are on the “defensive” side of investment-treaty negotiations. In practice, they are concerned that foreign investors will win BIT-related legal cases that would fail in US courts.

**Do you support the US-China BIT?**

Based on the 2004 model BIT, no. The legal risks for US-based companies are significant and should be thought through more thoroughly. A major mistake would be unintentionally giving China rights that domestic investors do not have, or freeing Chinese companies from obligations to which domestic companies are bound.

In the financial-services sector, for example, how would a Chinese sovereign wealth fund be regulated in the US in terms of minimum-equity requirements? In addition, it is possible that a Chinese SWF that invests in the US under the auspices of a US-China BIT could avoid future domestic regulatory changes in the financial sector, as it could argue under pre-existing law (that is, the BIT regulations) that it is not subject to new laws.

Risks to the US in terms of third-party involvement are also significant. For example, under the current US model BIT, a country that sets up a subsidiary in China would be given the same rights as a Chinese company when investing in the US. If that third country is one with which the US has shaky investment relations, this presents a troublesome scenario.

**What are the prospects for reciprocal market access within the framework of a US-China BIT (that is, use of a “negative list” by the US compared with a possible “positive list” by China)?**

A positive list is much easier to control than a negative list; for that reason, the interviewee prefers a positive list to negative one.

**What alterations to the model BIT would you advocate?**

Several main points come to mind in terms of investor rights. First is the issue of access to investor-state arbitration and the idea that, in this regard, one size does not fit all. The US model BIT, unlike the BITs of most countries, enables partner countries to pursue international legal routes before exhausting domestic (that is, US) legal options. The US should consider whether it is appropriate to give the same arbitration rights to all countries with which it negotiates BITs, and whether the implications of those arbitration rights will be the same for all investors within a market. In the context of China, the sheer size of the market means that Chinese-owned companies

could acquire a significant stake in major US companies. Is it wise to provide investor arbitration to those companies? It is also possible that state-owned enterprises in China could behave very differently from other companies in regards to handling of investment disputes with the US.

Second is the issue of BITs outsourcing constitutional law. The model BIT links minimum standard of treatment, which includes “fair and equitable treatment”, to the customary international law treatment of aliens. While this customary international law is in theory based on the general practice of states, in practice, an expanding and evolving approach to minimum standard of treatment has been taken in tribunals (one that is based on the decisions of other tribunals rather than the practice of states). In the long term, the asymmetry between foreign and domestic legal rights would put pressure on the US legal system to reform.

Third is the issue of preserving US policy space. As the number of BITs increases, and thus more investors are given arbitration rights, the risk that arbitrators will interpret the ambiguity of investor protections in ways that are unfavourable to the United States increases.

## **5. Thea Lee, Policy Director, AFL-CIO**

### **Do you support the US-China BIT?**

There are some concerns, some of which apply to all large developing economies (China, India and Russia have all initiated BIT negotiations with the US) and some of which are specific to China. In the case of China, the magnitude of the US trade deficit with China is a major concern. As it stands, many multinational companies have shifted portions of their operations to China; for US-based MNCs, this shift has had a detrimental impact on US jobs. It is possible that a US-China BIT will result in further negative impacts on US jobs (an even greater concern if worker rights are not better accounted for in the model BIT) and worsening of the trade deficit.

**I understand you were part of the subcommittee of the Advisory Committee on International Economic Policy that submitted a report on the model US BIT to the State Department and the Office of the United States Trade Representative several months ago. Would you summarise some of the main points you made in that report?**

There was a clear divide between environment supporters and labour supporters among the group that produced the report. Thea Lee’s main concern about that model BIT, apart from issues surrounding worker rights, is that the investor-state dispute-settlement mechanism now in the model US BIT gives too much power to foreign investors. The mechanism provides extraordinary rights to foreign investors but does not require commensurate responsibilities.

**Could you speak to the labour issues surrounding a US-China BIT in particular? How do those issues differ from labour issues related to other US BIT negotiations?**

As a formidable industrial power, China is a case of its own. Beyond sheer economic size, it is clear that China is in violation of worker rights and freedom of association among workers. For example, aside from the Chinese Communist Party-backed All-



China Federation of Trade Unions, unions are not allowed in China. And China does not enforce even existing legislation on minimum wage, health and safety, child labour and forced labour. These issues require serious attention if the US is to continue BIT negotiations with China.

**Do you have expectations for the macroeconomic impacts of a potential US-China BIT? Increased foreign direct investment, trade flows, etc.?**

While it is tough to estimate potential economic impacts, to the extent a BIT opens avenues for US multinational companies to relocate to or open branches or factories in China, there will be a clear negative impact on US jobs [given, presuming, lower operating and labour costs in China]. It is more difficult to assess the potential behaviour of Chinese firms if they were given greater capacity to invest in the US—would they hire local workers and source inputs locally, for example? In either case, US-China BIT negotiators should be concerned about the potential for accelerating the already very large US trade deficit with China.

## Appendix I: US BITs and date of entry into force

(1) Grenada	March 3rd 1989
(2) Cameroon	April 6th 1989
(3) Bangladesh	July 25th 1989
(4) Congo	July 28th 1989
(5) Turkey	May 18th 1990
(6) Senegal	October 25th 1990
(7) Morocco	May 29th 1991
(8) Panama	May 30th 1991
(9) Egypt	June 27th 1992
(10) Czech Republic	December 19th 1992
(11) Slovakia	December 19th 1992
(12) Tunisia	February 7th 1993
(13) Sri Lanka	May 1st 1993
(14) Kazakhstan	January 12th 1994
(15) Kyrgyz Republic	January 12th 1994
(16) Romania	January 15th 1994
(17) Bulgaria	June 2nd 1994
(18) Poland	August 6th 1994
(19) Congo Brazzaville	August 13th 1994
(20) Argentina	October 20th 1994
(21) Moldova	November 25th 1994
(22) Armenia	March 29th 1996
(23) Ukraine	November 16th 1996
(24) Latvia	November 26th 1996
(25) Trinidad and Tobago	December 26th 1996
(26) Mongolia	January 1st 1997
(27) Estonia	February 16th 1997
(28) Jamaica	March 7th 1997
(29) Ecuador	May 11th 1997
(30) Georgia	August 17th 1997
(31) Albania	January 4th 1998
(32) Bahrain	May 31st 2001
(33) Bolivia	June 6th 2001
(34) Croatia	June 20th 2001
(35) Honduras	July 11th 2001
(36) Azerbaijan	August 2nd 2001
(37) Lithuania	November 11th 2001
(38) Jordan	June 13th 2003
(39) Mozambique	March 3rd 2005
(40) Uruguay	November 1st 2006

## **Appendix II China BITs and date of entry into force**

- (1) France May 30th 1984
- (2) Norway November 21st 1994
- (3) Singapore November 21st 1985
- (4) Thailand March 12th 1985
- (5) Kuwait November 23rd 1985
- (6) Austria September 12th 1985
- (7) Denmark April 29th 1985
- (8) Italy January 28th 1985
- (9) Sri Lanka March 13th 1986
- (10) Switzerland November 12th 1986
- (11) United Kingdom May 15th 1986
- (12) Japan August 27th 1988
- (13) New Zealand November 22nd 1988
- (14) Malaysia November 21st 1988
- (15) Poland June 7th 1988
- (16) Australia July 10th 1988
- (17) Ghana October 12th 1989
- (18) Bulgaria June 27th 1989
- (19) Pakistan February 12th 1989
- (20) Russia July 21st 1990
- (21) Turkey November 13th 1990
- (22) Mongolia August 25th 1991
- (23) Papua New Guinea April 12th 1991
- (24) Hungary May 25th 1991
- (25) Armenia July 4th 1992
- (26) Kazakhstan August 10th 1992
- (27) Kyrgyz Republic May 14th 1992
- (28) Moldova November 6th 1992
- (29) Turkmenistan November 21st 1992
- (30) Ukraine October 31st 1992
- (31) Uzbekistan March 13th 1992
- (32) South Korea September 30th 1992
- (33) Argentina November 5th 1992
- (34) Bolivia May 8th 1992
- (35) Philippines July 20th 1992
- (36) Vietnam December 2nd 1992
- (37) Greece June 25th 1992
- (38) Albania February 13th 1993
- (39) Belarus January 11th 1993
- (40) Croatia June 7th 1993
- (41) Georgia June 3rd 1993
- (42) Tajikistan March 9th 1993

- (43) Uruguay December 2nd 1993
- (44) Laos January 31st 1993
- (45) United Arab Emirates July 1st 1993
- (46) Estonia September 2nd 1993
- (47) Lithuania November 8th 1993
- (48) Slovenia September 13th 1993
- (49) Egypt April 21st 1994
- (50) Azerbaijan March 8th 1994
- (51) Romania July 12th 1994
- (52) Chile March 23rd 1994
- (53) Ecuador March 21st 1994
- (54) Jamaica October 26th 1994
- (55) Peru June 9th 1994
- (56) Indonesia November 18th 1994
- (57) Iceland March 31st 1994
- (58) Morocco March 27th 1995
- (59) Serbia and Montenegro December 18th 1995
- (60) Cuba April 24th 1995
- (61) Israel April 10th 1995
- (62) Oman March 18th 1995
- (63) Algeria October 17th 1996
- (64) Mauritius May 4th 1996
- (65) Zambia June 21st 1996
- (66) Zimbabwe May 21st 1996
- (67) Bangladesh September 12th 1996
- (68) Cambodia July 19th 1996
- (69) Lebanon June 13th 1996
- (70) Saudi Arabia February 29th 1996
- (71) Syrian Arab Republic December 9th 1996
- (72) Cameroon May 10th 1997
- (73) Congo, December 18th 1997
- (74) Gabon May 9th 1997
- (75) South Africa December 30th 1997
- (76) Sudan May 30th 1997
- (77) Macedonia, June 9th 1997
- (78) Yemen February 16th 1998
- (79) Cape Verde April 21st 1998
- (80) Ethiopia May 11th 1998
- (81) Barbados July 20th 1998
- (82) Belize January 16th 1999
- (83) Bahrain June 17th 1999
- (84) Qatar April 9th 1999
- (85) Botswana June 12th 2000
- (86) Congo March 20th 2000
- (87) Brunei November 17th 2000

- (88) Iran July 22nd 2000
- (89) Kenya July 16th 2001
- (90) Mozambique July 10th 2001
- (91) Nigeria August 28th 2001
- (92) Sierra Leone May 16th 2001
- (93) Myanmar December 12th 2001
- (94) Jordan November 15th 2001
- (95) Cyprus January 17th 2001
- (96) Netherlands November 26th 2001
- (97) Côte d'Ivoire September 23rd 2002
- (98) Bosnia and Herzegovina June 26th 2002
- (99) Trinidad and Tobago July 22nd 2002
- (100) Djibouti August 18th 2003
- (101) Guyana March 27th 2003
- (102) Germany December 1st 2003
- (103) Benin February 18th 2004
- (104) Tunisia June 21st 2004
- (105) Uganda May 27th 2004
- (106) Finland November 15th 2004
- (107) Latvia April 15th 2004
- (108) Sweden September 27th 2004
- (109) Equatorial Guinea October 20th 2005
- (110) Guinea November 18th 2005
- (111) Madagascar November 21st 2005
- (112) North Korea March 22nd 2005
- (113) Belgium/Luxembourg June 6th 2005
- (114) Czech Republic December 8th 2005
- (115) Portugal December 9th 2005
- (116) Slovakia December 7th 2005
- (117) Spain November 14th 2005
- (118) Namibia November 17th 2005
- (119) Vanuatu April 7th 2006
- (120) India November 21st 2006